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How The Year 2000 Bug Will Hurt The Economy

(It's worse than you think)

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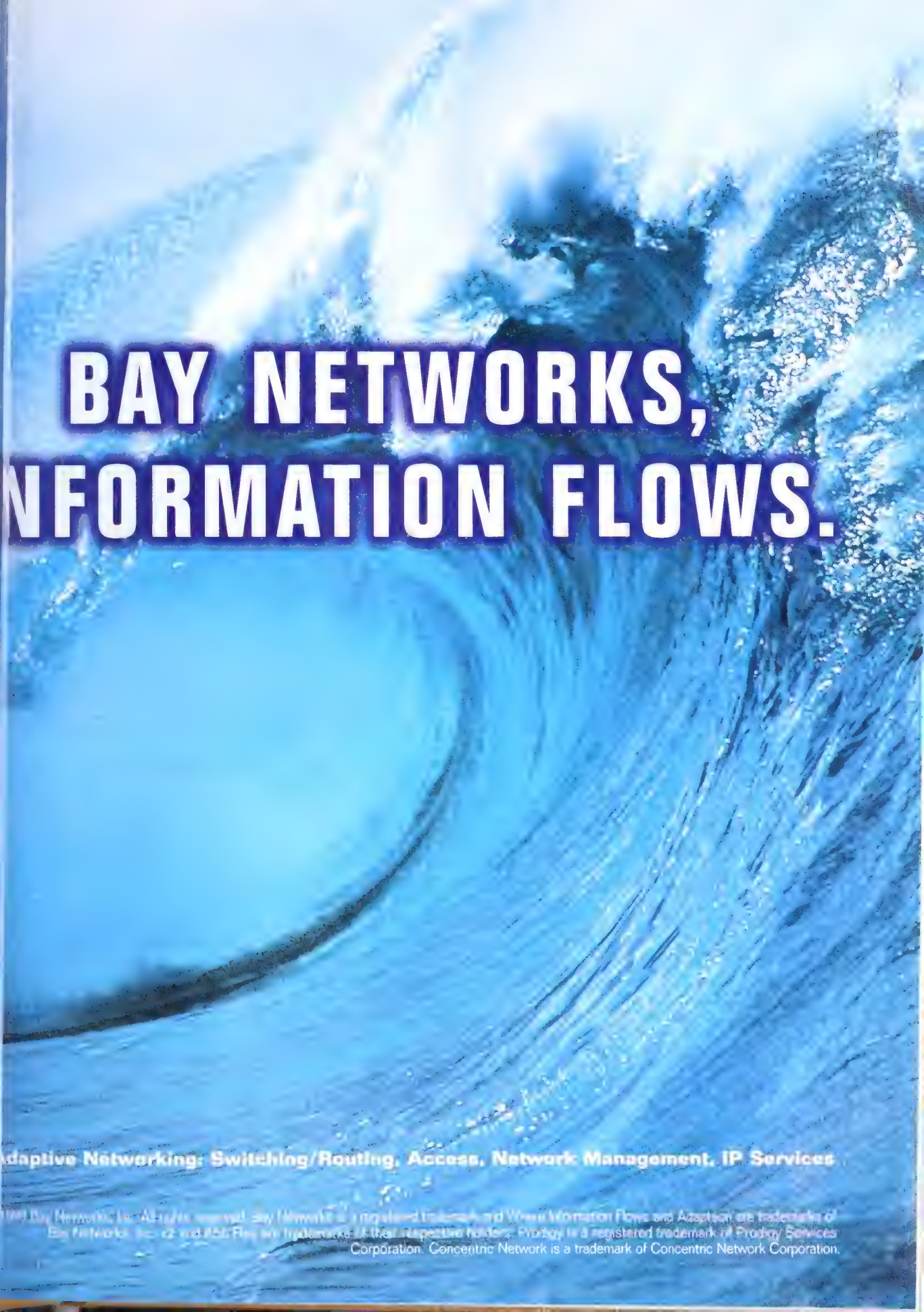
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COVER STORY

ZAPPED BY YEAR 2000

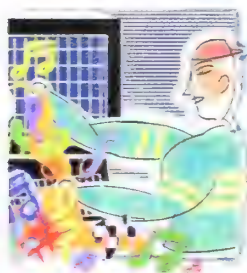
The Millennium Bug is set to take a big chunk out of growth—and is already having an impact **page 12**

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NET FRENZY

Companies race to offer the grandest portals **page 73**



DOWNLOADING MUSIC

Can the music biz chase pirates and get in on Net distribution, too? **page 89**



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From banks to nuclear plants, a lot of companies and government agencies are about to get zapped: They're unprepared for Y2K, the mother of all computer glitches. System malfunctions, along with sidetracked workers and funds, will push growth down and inflation up. The economy is in for its first global high-tech shock

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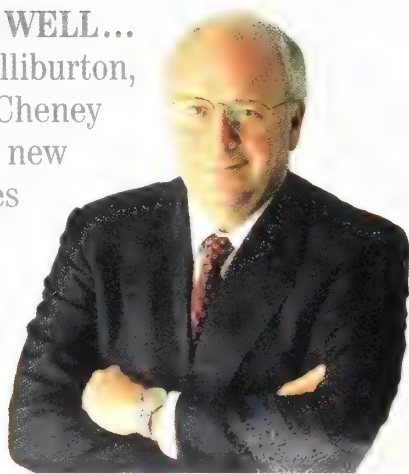


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Up Front

EDITED BY ROBERT McNATT & LARRY LIGHT

RETAIL TALES

FRENCH FRIES OR CHINA GROWTH?

HERE'S SOME REAL OVER-THE-counter marketing. As a Mar. 2 deadline for a popular IRA-like savings plan nears in Canada, the Bank of Montreal and McDonald's are teaming up to pitch mutual funds. Diners at 400 Golden Arches outlets in Ontario recently got brochures asking: "Would you like some mutual funds with that?" Their reward for filling out the flier: a free coffee, muffin, and telemarketer's call.

Mixing Macs and mutual funds, some marketing pros say, may not make for a happy meal. The University of Toronto's Scott Hawkins worries that the venture will hurt the bank's image. Others doubt the promo will do McDonald's any good, saying funds don't appeal to its market as do, say, kids' movies. Another issue: Are naifs be-



ing lured into risky investments? Bank officials argue that they have many conservative funds. Besides, they say, McDonald's customers, a societal cross-section, are as sophisticated as anyone.

The bankers, encouraged, expect 75,000 responses. Harris Bank in Chicago, owned by Bank of Montreal, is mulling the idea in the U.S. with someone. But so far, McDonald's in the States isn't biting. *Joseph Weber*

THE FUND FRONT

DUMPING A STOCK BEFORE ITS TIME

SOME MUTUAL-FUND FAMILIES have stumbled recently, having the bad fortune to dump their Computer Sciences stock before Computer Associates launched a \$108-a-share hostile bid on Feb. 17.

Among the big losers is Fidelity Investments. It held 5.7 million shares of CSC a year ago and sold all but 429,000 of them by November. The situation is even worse at Janus, which said it sold its

entire CSC stake of 6.1 million shares in 1997. That's bad news. CSC was trading in the low 80s in early 1998.

Still, there are some likely winners. Stockpicker G. Kenneth Heebner's New England Growth Fund is sitting pretty with 818,000 CSC shares. The nicest chunk of change, however, may accrue to American Express Financial Advisors, which includes the IDS funds. On Dec. 31, it held more than 4.9 million CSC shares. An AmEx executive wouldn't say if any CSC has since been unloaded. But if it hasn't, that stake is now worth an additional \$120 million. *Robert Barker*

FUND HOLDINGS OF CSC SHARES

AMERICAN EXPRESS (12/31/97)	4,900,000
NEW ENGLAND GROWTH (11/30/97)	818,000
FIDELITY (10/31/97)	429,000
JANUS (2/17/98)	0

TALK SHOW "Maybe there'll be a simple, innocent explanation. I don't think so, because I think we would have offered that up already."—*White House press secretary Mike McCurry, trying to explain the Clinton-Lewinsky relationship. Late he said he goofed when he made the statement.*

CORPORATE COUPLINGS

BELL ATLANTIC, GTE COME A-COURTIN' SPRINT

IN EARLY FEBRUARY, SPRINT Chairman William Esrey declared publicly and loudly that the country's third-largest long-distance company was not for sale. However, just because he doesn't want to sell doesn't mean other companies don't want to buy.

GTE and Bell Atlantic are now independently considering bids for the long-distance carrier that could come within the next several weeks, say sources close to both companies. The two telecom giants are talking to investment bankers about all-stock bids for Sprint that would likely exceed \$30 billion.

The strategic value of a deal is compelling for both

companies. GTE has been pushing into the long-distance business, but its effort has been expensive and has generated only 1.7 million customers. Meanwhile, Bell Atlantic, which recently merged with Nynex, has long wanted to expand nationally.



SPRINT'S ESREY

Still, a Sprint deal is far from certain. France Telecom and Deutsche Telekom, which together own 20% of the U.S. carrier, could block it. Esrey is willing to sell at all, he would demand a hefty premium. That would likely mean at least 25% over Sprint's current share price, about \$30. Bell Atlantic and Sprint declined to comment. A GTE spokesman could not be reached. *Peter Elstrom*



HONCHOS

WHY THE CEO MAY BE WORTH \$100 MILLION

EARNINGS MAY BE SOARING for some companies, but does that justify a CEO's taking home, as Walt Disney's Michael Eisner did last year, more than \$100 million after cashing in his stock options?

Those fat payouts—and Eisner's came after taxes, charitable gifts, and buying more stock—may just be worth it, say Brian Hall and Jeffrey Liebman, two Harvard University professors

who studied executive pay for the National Bureau of Economic Research. They found that comp is indeed linked to performance, thanks to options. "The incentive effect of stock options is 10 times that of salary and bonus," says Hall. He adds that salary and bonuses change much less in relation to company performance, as measured by stock price.

After looking at data from large public companies from 1980 through 1994, the authors also found that the most recent correlation between pay and performance was about three times what it was in the 1980s. The implication, says Hall, is that CEOs should be paid with even more options. Compensation and performance shouldn't fully work in lockstep, he adds, "but compared with 15 years ago, we've made enormous progress."



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Up Front

REALITY BYTES

GUESS THE CHECK IS IN THE E-MAIL

YO, BILL! WHERE'S MY \$1,000? That's what hundreds of irate cybernauts have demanded of Microsoft Chairman Bill Gates after apparently getting E-mail from him. The bogus missive offers the cash—or a free copy of Windows 98—if recipients forward his message to 1,000 people and test some new software.

The chain letter, one of a string of pranks at the software giant's expense, bears a Microsoft return address, fooling some people into thinking it's real. The company says the hoax has hit college campuses and, if the past is any guide, should soon appear in corporate offices.



GATES: Prank victim

Microsoft has seen worse. In Brussels recently, a mischief-maker threw a cream pie in Chairman Bill's face. Then, just as the company

began beta-testing Windows 98, the gagsters at Palladium Interactive released a software parody, *Microshaft Corp. Winblows 98* (Motto: "GET SHAFTED"). The prank that has generated the biggest E-mail response to Microsoft, though, is the chain letter. The company says

about half the messages express anger about getting unsolicited commercial E-mail; the rest want the money. Nobody, it seems, asks for Windows 98. *Roy Furchgott*

OVER THERE

MY, YOUR EXHAUST SMELLS DELICIOUS



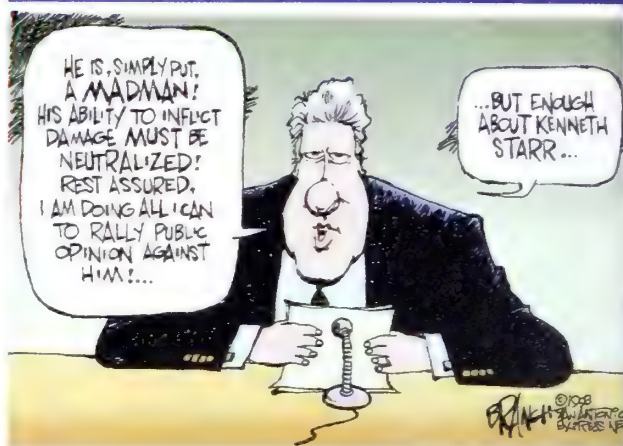
French fries, are already a source of deep gastronomic pride in that country, where residents love to devour them with a dollop of garlicky mayonnaise. But scientists say there is an even better reason for folks to keep eating them. They say they can now use discarded french-fry grease to make cleaner-burning diesel fuel.

Yes, the oil they cook with could actually end up in their

gas tanks. The Flemish Institute of Research says a specially treated mixture of 20% french-fry oil and 80% regular diesel fuel will cut carbon-monoxide pollution by one-fifth. And as a bonus, the institute says the new fuel, which can be made from different vegetable oils, leaves an odor redolent of fries.

But don't put your nose to the tailpipe quite yet. Belgium's PetroFina oil company says making the eco-friendly stuff still isn't cost-effective, so it's asking for government subsidies or tax breaks. Says project leader Luc Pelkmans: "Belgium has a lot of good leftover oil, and this is a way of recycling it." Now, how about a new use for old mayonnaise? *William Echikson*

DRAWN & QUARTERED



PRODUCT PEEK

VOICES IN YOUR KID'S HEAD

FORGET BEANIE BABIES AND Tomogochi toys. According to OddzOn, a division of Hasbro, the next hot plaything for kids will be a lollipop holder. Of course, in this interactive age, that means more than just a white paper stick: OddzOn has developed Sound Bites, a holder that plays music audible only to the lollipop-licker.

Sound Bites, for children 4 and up, sports a \$9.95 retail price and is expected to be in stores soon. After a lollipop is inserted into it, the gizmo works by producing wacky sounds or instrumentals from a tiny speaker. The beauty part is that the vibrations supposedly migrate up the stick to resonate in the candy-

SECRET SONG:
Only the lollipop lick
can "hear" vibration

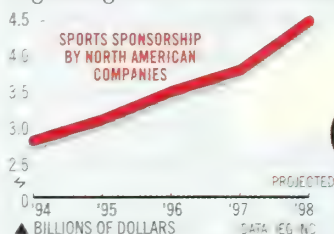
earer's teeth, jaws, and ears, so that no one else hears the saxophones, drums, or battling spaceships.

"This is how you hear your own voice inside your head," says co-inventor David Capper—just in case you wondered. He adds that Sound Bites, praised the likes of F.A.O. Schwarz CEO John Eyler, has already been approached by several licensees. All apparently want the chance to set their own pop tunes a theme songs deep into a child's teeth. *Kathleen Mor*

THE BIG PICTURE

WE'D LIKE TO THANK OUR SPONSORS

The Nagano Olympics' corporate logos cost a bundle. Companies increasingly are paying to sponsor everything from sandlot softball to marathons. Sports gets two-thirds of all sponsorship spending, which is growing faster than advertising.



FOOTNOTES Average percentage of junk-bond issues in default: of those floated from 1984-90, 33%; from 1991-97, 9%

Rhône-Poulenc: 1997 results

"The objective for 20% growth in 1997 net earnings per share excluding non-recurring charges, has been met with a rise of 20.62%.

1997 was a very important year for Rhône-Poulenc: we consolidated our activities in the Life Sciences and paved the way for the creation of Rhodia with its business portfolio sharply focused on specialty chemicals. These operations led to a non-recurring charge of FF9.7 billion carried in 1997 accounts, which is reflected in a net loss for the year.

Enhancing the value of the Group remains our priority. We aim to achieve a return on equity of 13% by the year 2000.

To achieve this, the Group is counting on new products in the Life Sciences and on Rhodia's future development. We also intend to improve the earnings potential of our businesses. That is why new operations will be launched in 1998, which will result in additional non-recurring charges in the region of FF2 billion.

For 1998, we are maintaining our target of 20% growth in net earnings per share, excluding non-recurring charges".

Jean-René Fourtou
Chairman and Chief Executive Officer

Consolidated results

Net sales:
FF89.995 billion (+11.4%)*
Net loss: FF4.991 billion
Net income excluding non-recurring charges: FF3.417 billion (+24.7%)

Life Sciences

Consolidated net sales:
FF52.6 billion (+11.7%)*
Earnings from operations:
FF8.4 billion (+0.95%)

Pharmaceuticals

Consolidated net sales:
FF33.3 billion (+10.8%)*
Earnings from operations:
FF5.3 billion (-7.9%)

The downturn in earnings for pharmaceuticals is primarily due to the Centeon situation and to the decline in sales of asthma products in the United States, as well as weaker demand on the French pharmaceuticals market.

**Rhône-Poulenc,
a worldwide leader
in life sciences,
and its
specialty chemicals
subsidiary,
Rhodia,**



**contribute
through innovation
to enhancing
human well-being
from health
and food to the
quality and safety
of products
used in
every day life.**

In contrast, strong growth was recorded in new product sales, particularly in the United States: Clexane®/Lovenox®, the world's leading product for the prevention of deep vein thrombosis; Taxotere®, the anti-cancer agent available in 55 countries; Rilutek®, the only available treatment for ALS (amyotrophic lateral sclerosis or motor neuron disease); Nasacort/AQ® for allergies.

Strong sales growth in vaccines helped consolidate Pasteur Mérieux Connaught's worldwide positions, particularly in the United States (Ipol®, an injectable polio vaccine and Tripedia®: pertussis, diphtheria, tetanus).

■ Plant and Animal Health

Consolidated net sales:
FF19.5 billion (+12.8%)*
Earnings from operations:
FF3.1 billion (+20.5%)

Growth was fuelled by a generally buoyant market, the rapid increase in new product sales and the earnings posted by Merial. Frontline®, an antiparasitic agent for animals, recorded sales up 150% in 1997.

Regent®, the brand name of the new Fipronil-based insecticide, doubled its 1996 sales performance.

In animal nutrition, methionine and vitamins continued to improve their sales performance (up by 10%).

Chemicals/Fibers and polymers

Consolidated net sales:
FF37.5 billion (+10.6%)*
Earnings from operations:
FF2.1 billion (+76%)

The increase is mainly due to enhanced sales in most businesses.

The refocusing process toward specialty chemicals continued. The Chemicals and the Fibers/polymers businesses were merged into a new company, Rhodia, on January 1, 1998.

A gross dividend per ordinary "A" share of FF5.62 (FF5.25 in 1996) will be recommended by the Board of Directors at the Annual General Meeting of Shareholders to be held on May 26, 1998.

* On a comparable Group structure

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First quarter 1998 results: April 30, 1998.



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If you think the *AmericaOne* team is a bunch of tan yachtsmen pulling lines and unfurling sails, you probably haven't followed the sport since the late 1800s. Today's America's Cup challengers have more than a rudimentary knowledge of disciplines like fluid dynamics and automated design systems. Which is why the formidable *AmericaOne* team uses Quantum Atlas II disk drives for their complex 3D analyses of hull, keel and sail designs. Of which there are tens of thousands. No problem for the incredibly reliable Atlas II. Its high performance input/output and storage capacity enables design teams to study more possible configurations than ever before. For more information on the Atlas II and the full line of Quantum storage solutions, call us at 1-800-624-5545, extension 142. Or visit our website at www.quantum.com. Oh, and if you're searching for the *AmericaOne* team, just look for the America's Cup. There's a good chance they'll be holding it.

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KEEPING AIR FARES GROUNDED WITHOUT A LOT OF RED TAPE

Regarding "Prying open the open skies" (News: Analysis & Commentary, Feb. 9): More regulation? Please, no! Regulation was the hallmark of the years up to the 1980s, and since this burden was lifted, everything from telephones to trucking is more reliable, with more choices at lower cost. We need less regulation and more enforcement of existing antimonopoly laws to give competition a chance.

Try this: Any airline that holds more than 66% of the traffic on a route should be able to change prices and fare categories only once a year on that route. Simple enough. What it means is that Delta, for example, would be locked into its pricing for all fare groups for a full year on the Tampa-Atlanta route, forcing it to either hold a reasonable price or allow a competitor a year to operate without fear of predatory pricing.

J. B. Caswell
Chairman
Omnia Group Inc.
Tampa

THOSE FALLING OIL PRICES HAVEN'T HIT BOTTOM YET

Readers of "How low can oil prices go?" (News: Analysis & Commentary, Feb. 2) should also note two additional developments that will contribute to low petroleum prices. First, the impact of the Asian economic crises will increase supplies of petroleum products as well as reduce demand. Indonesia and Malaysia, both oil and gas producers hard hit by currency woes, are expanding production to generate crucial export earnings. Thailand is pushing forward on offshore development projects for the same reason.

Second, Iraqi oil sales may well increase significantly, subject, of course, to the outbreak of hostilities. The U. N. has now proposed terms than doubling Iraqi oil sales under the Food for Oil Program to \$5.2 billion every six months. Iraq is entitled to sell oil under

CORRECTIONS & CLARIFICATIONS

A table accompanying "A revolution in pain relief?" (Science & Technology, Feb. 1) should have read that Johnson & Johnson product was in phase 2 clinical trials.

the program up to a fixed U.S. dollar amount, whether the existing \$2 billion ceiling or any higher ceiling the U.S. Security Council may adopt. If per barrel prices continue to drop, then Iraq is entitled to increase production to store its sales revenue to the maximum amount permitted.

Mark Kan
Milbank, Tweed, Hadley & McC
Washing

GIVE FASB CREDIT FOR WARNING ABOUT STOCK OPTIONS

There is striking irony in Jennifer Reingold's article, "Accounting changes that keep investors in the dark" (News: Analysis & Commentary, Feb. 9). In 1990, the Federal Accounting Standards Board (FASB) tried to do the right thing on stock options in the face of pressure from corporations, the business press, and accounting firms. Ultimately, facing a threat from Congress, FASB reluctantly issued its current ruling, while noting that it still believed flawed in not recognizing compensation in the form of stock options. It is interesting that it is now held to blame for the resulting bad accounting.

Mark La
Kenan-Flagler Business School
University of North Carolina
Chapel Hill, NC

AUTONATION NEEDS TO SHIFT GEARS AGAIN

AutoNation USA is rapidly becoming that which it sought to overcome ("The public learns cars ain't videos," The Corporation, Feb. 9). The sales staff, who was originally salaried, now works on commission (translation: higher pr

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Moreover, consumers are benching the fixed prices at AutoNation when using that as a basis for negotiation at competitors' locations. Thus, competitors are the true benefactors of Nation's presence and have generated more sales in markets where AutoNation has entered.

AutoNation only addressed the upside of the equation. Now it must address the demand side to become a term player in the used-car arena.

Stuart H. Angert

CEO

Marketing Services of America Inc.
Amherst, New York

TON, THE PRESIDENCY, AMERICAN OPINION

Our editorial, "How do we explain to our children?" (Editorials, Feb. 9) did not have the effect intended. I heartened to learn that for once Americans are thinking for themselves. No one is applauding the President's behavior, actual or imagined, but there are some matters that are too embarrassing to the American public to appear in large, front-page print. Moreover, Clinton has done nothing that any of his predecessors have not also

The media of the past had a respect for the privacy of the individual that is missing today. We routinely stick microphones into the faces of the newly bearded and disrespect the Presidency by revealing facts about the man that do not reflect his ability to govern. What we have done is make our country and its President seem petty. Sex indiscretion, unfortunately, is as common in government as it is elsewhere. If we penalize the President, then let's demand the resignation of every elected official, CEO, and world leader—and if not, who would be left?

Angela P. Scott
Philadelphia

I no longer feel isolated and confused. Until the point when I read your comments, I was becoming more and more frustrated over the current state of affairs in the White House, and I needed to be the only one concerned about it. But you hit the nail on the head as you expressed confusion over the disturbing results of the latest polls regarding a public view of "It's his personal life, leave him alone."

Whether the questions were designed to lead to those conclusions, or we Americans are truly lethargic about misbehavior in this nation's most respected

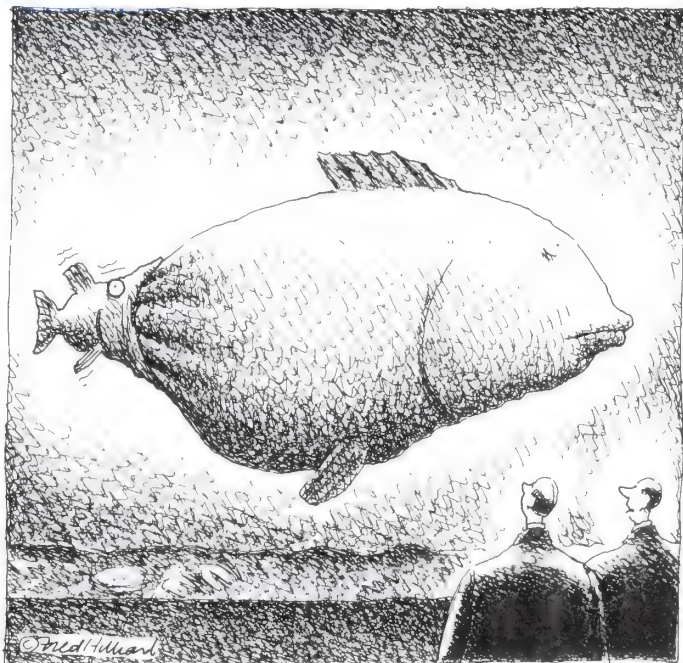
office because our tummies and pocketbooks are full. BUSINESS WEEK is not prudish or naive to find this U.S. apathy worrisome. If this nation is to maintain its strength and respect throughout the world, then we must demand a moral and ethical leader. Anything less compromises our great nation.

Dale Hedges
Santa Ana, Calif.

DID BRITISH PETROLEUM POLLUTE ALASKAN POLITICS?

Jeffrey E. Garten's article, "Globalism doesn't have to be cruel" (Economic Viewpoint, Feb. 9), advises us that British Petroleum Co. has done well financially even while doing good. He quotes John Browne, CEO of BP: "We have to be acutely conscious of our lim-

WillTales

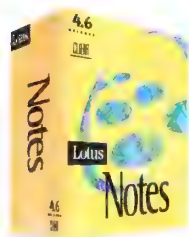


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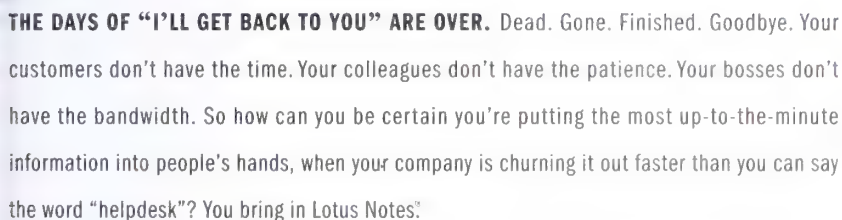
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Arndt von Hippel
Anchorage, Alaska

A CREATIVE PROPOSAL FOR KEEPING IRAQ IN LINE

Iraq should pay the price for not complying with U.N. resolutions ("Iraq: Would the U.S. be bombing itself in the foot?" International Outlook, Feb. 9). An alternative to bombing would be to carve out a chunk of land from Iraq, say 20%, to form a new country if Saddam continues to deny full inspections.

It could be called New Iraq or Free Iraq, controlled by members of the Arab countries with no U.S. intervention except oversight. Oil could be sold, with a large percentage of the profits retained by the new country; the rest could be a management fee earned by Arab countries. If Saddam continued to resist inspection, the land percentage forfeited would be increased. U.S. involvement would be limited to military support as directed by the Arab countries.

This way, Saddam could save face with his people while complying with the required inspections. And a military solution is avoided, and the heavy hand of the U.S. wouldn't hinder our relations with the Arab nations.

Pete Barbaro
New York

ANOTHER VIEW ON THAT CONTROVERSIAL TRADE DEAL

Paul Magnusson's article "The explosive trade deal you've never heard of" (Washington Outlook, Feb. 9) is an ill-informed attack on an important negotiation intended to secure the benefits of foreign investment by establishing a set of internationally agreed-upon rules.

The Multilateral Agreement on Investment (MAI) is important to U.S. business. We want a high-standard multilateral agreement to ensure the free flow of investment by preventing discriminatory treatment against investors, protecting those investments against expropriation, giving investors

access to dispute settlement procedures, and lowering barriers to investment.

There is nothing in the current MAI—or anything contemplated—that would enable a firm to disregard a host country's environmental, labor, or social laws. Nor does the proposed agreement cover trade sanctions, so the claim that the MAI would bar use of such measures to stop human-rights abuses or other nefarious practices is preposterous. And the MAI will not require a rollback of existing state laws involving, for example, minority set-asides and enterprise zones. Existing laws will remain in force and cannot be challenged under the MAI's dispute-settlement mechanism.

Even though MAI will go to the Senate as a treaty, the House will review it because of the need for implementing legislation. Congressional hearings on the MAI may be the only way to separate fact from fantasy and expose the wild claims of some groups to public scrutiny.

Timothy E. Deal
Senior Vice-President
U.S. Council for International Business
Washington

THE VIACOM-FOX AFFAIR: A JUDGE WEIGHS IN

In "Caught: A job-hunter. Penalty: House arrest," (News: Commentary & Analysis, Jan. 12), Elizabeth Lesly Stevens mischaracterized the crux of Viacom's MTV Networks' lawsuit against Fox Kids and Richard Cronin. She concluded that "Viacom is way out of line." It's Stevens who was out of line, which was made clear when Judge Herman Cahn upheld MTVN's position on Feb. 4.

Stevens' analysis would have readers believe that this suit was about intimidating employees from having "exploratory discussions" with prospective employers, or about Viacom trying to get a cut of Cronin's future. But the judge agreed with MTVN that signing a contract and accepting future stock options from a competitor—more than eight months before his current contract as president of Nick at Nite's TV Land expired—rendered Cronin untrustworthy to do his job. The judge pointed out that by Cronin's own admission, there were areas of his MTVN job in which he would no longer be able to function effectively—particularly strategic issues relating to competition with Fox Kids.

The judge found that MTVN was justified in terminating Cronin for breaching his contract and deserved the in-

junctive relief sought. The court ruled that Cronin could not go to work for Fox Kids before July 1 at the earliest. What Fox Kids and Rich Cronin attempted to do is far from "common practice." It was just plain wrong.

Michael D. Frickel
Deputy General Counsel

Viacom Inc.
New York

Editor's note: The full case is still awaiting trial. On Feb. 4, the judge granted an injunction barring Cronin from starting work for a competitor until his previous employment contract with Viacom expired. We agreed with Viacom's argument that Cronin not be allowed to compete with Viacom for the duration of his contract term. We disagreed with Viacom on other issues, including its view that it has a right to any rise in the value of the Fox assets Cronin will oversee.

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MACHINE BEAUTY
Science and the Heart of Technology
 David Gelernter
 c Books • 166pp • \$20

WHAT'S SO SCARY ABOUT GOOD DESIGN?

Americans love technology, but they feel a little queasy about beauty. That's a real problem, according to David Gelernter, the Yale university computer science professor and author of *Machine Beauty*. "Insist that beauty is at the heart of science and technology is like ordering a steak at lunch, or tacking ruffles to your coffee furniture—it takes a serious position and makes it frilly and frivolous," he writes.

But Gelernter does insist that beauty should inform the way we conceive of and build machines. If the author had his way, all computer scientists and software engineers would be sent off to crash courses in drawing, design, and art history. Give every computer scientist a grounding in Michelangelo and Matisse, Gelernter believes, and software and hardware would be more beautiful and more functional. It's the aesthetics of the sort endorsed by such modern architects as Mies van der Rohe and Philip Johnson are a main theme of this disorderly but fascinating treatise—a book that also takes up such wide-ranging topics as the future of computing and the shortfalls of American taste, training, and education.

"Machine beauty" entails an inspired mingling of "simplicity and power," the author writes, citing as backup some timeless technological feats: the Hoover vacuum, the Empire State Building, and the 1938 J3 steam locomotive. Then he turns to one of the most ubiquitous machines of the Modern Age, the computer, which started out as a classic example of sophisticated simplicity: It harnessed the power of zeroes and ones to perform an almost infinite number of calculations and tasks. Gelernter's history of computers is interesting and accessible without being simplistic.

One modern computer achieved a high degree of machine beauty: the origi-

nal Apple Macintosh. Employing technology developed at Xerox Corp.'s Palo Alto Research Center, the Mac's interface was designed to look and act like a virtual office, with file folders and trash cans and an area in which you could work simultaneously in several different program "windows." It was straightforward and manageable, a happy contrast to rival Microsoft Corp.'s user-hostile DOS. Remember the sorry days when a user command might result only in a computer response of "Abort, retry, fail?" Or the terrifying "Fatal error"?

Yet even before it switched to Windows, Microsoft's ugly system overwhelmed Apple's machine beauty. How Microsoft managed to pull off this feat is hardly a new story—price, advertising, IBM market dominance, and the clones were all involved—but Gelernter believes there's a perplexing aesthetic angle involved here, too. Microsoft's Windows is almost a carbon copy of Apple's system. Did beauty ultimately triumph? Yes and no, Gelernter thinks, asserting that "it is possible" that "right up to the moment people fell in love courtesy of Microsoft with Apple-style beauty, they were repelled by it." One factor behind this "beauty paradox," he feels, is a kind of sexual discrimination: Some Americans, particularly those in business, didn't like Macintoshes because their very simplicity meant they were too girly or "sissy." The IBM PC, on the other hand, was, in the words of one technology columnist, "a man's computer designed by men for men."

Other factors as well may discourage an appreciation of machine beauty. Their very success has convinced many people that science and technology, as opposed

to the arts, "are the only intellectual attainments that count." Then, too, there are America's schools and colleges, which have ceased to offer a well-rounded education.

Gelernter complains that software makers are always adding useless bells and whistles, including clocks that announce they are on "U.S./Eastern" time, as if the user didn't know where he was. And since the chances that software will have bugs increase with its complexity, complicated software is often neither beautiful nor user-friendly. As an alternative, Gelernter promotes a project he and his graduate students have been developing called Lifestreams, which would provide a multimedia archive of a person's life that one can tap into just about anytime, anywhere.

Nor is Gelernter pleased with current computer hardware. "Almost every office in the country centers on an electronic Model T," he says, calling current desktops "graceless, lumpy objects."

As substitutes, he offers his own sketches of computers "made of warm orange wood, cherry or mahogany."

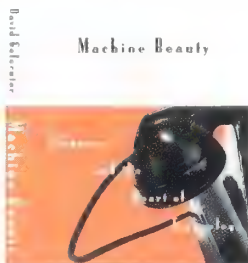
Gelernter is an engaging and amusing writer, even when he turns his hand to such a potentially dry topic as computer science. Unfortunately, there are times when his narrative wanders aimlessly. At other moments, the book seems to cry out for a red-pencil-

wielding editor. In a section attacking the notion that science is merely a social construct and not "a strong, hard, objective business," Gelernter writes that "any child... can see that the wavelength of blue light is the same in New York and Nigeria... that sine waves were shaped like sine waves yesterday afternoon and ten centuries ago." Any child? Any reader can see that such matters aren't child's play.

Despite its quirkiness and perambulations, *Machine Beauty* is an interesting, informative, and quick read. Who knows, Gelernter just might persuade some designer to put a little more Matisse in his next mouse—and we would all be the better for that.

BY SUSAN JACKSON

Connecticut correspondent Jackson prefers Degas to DOS.



David Gelernter

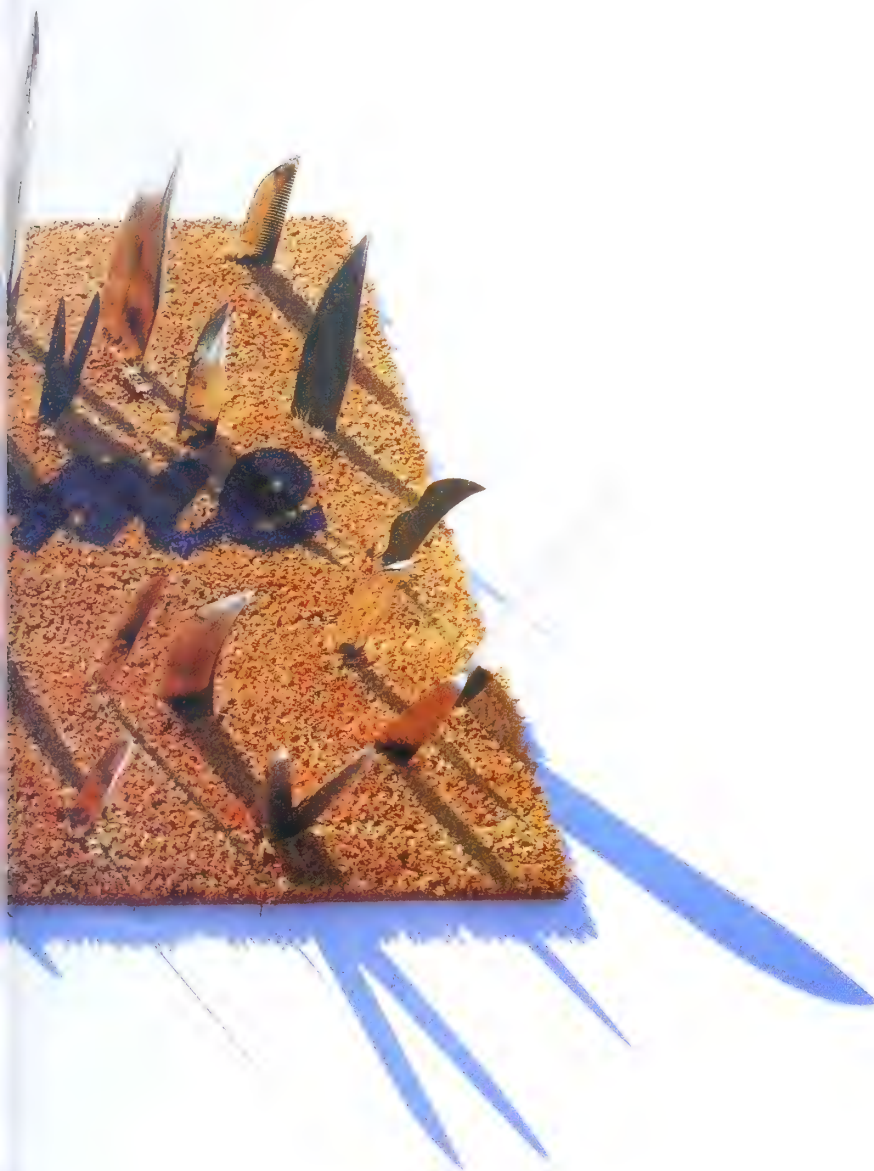
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HOT TYPE

IN AN AGE OF 800-PAGE BIOGRAPHIES, JACK Beatty has taken an admirable gamble: that he can describe the work and life of management guru Peter F. Drucker, and persuade readers of Drucker's greatness, in a mere 200 pages. The concept is attractive enough to have won the No. 6 spot on this month's hardcover best-seller list for *The World According to Peter Drucker*.

But Beatty fails on several counts. He considers most of Drucker's 29 books. But examinations of such early works of social and political analysis as *The End of Economic Man* and *The Future of Industrial Man* include little intellectual context and make Drucker's efforts sound muddled and derivative.

Soon, Drucker abruptly turned to investigations of Corporate

America. Why this sudden shift in method and subject matter Beatty offers little explanation.

In such efforts as *The Concept of the Corporation* (1949) Beatty shows Drucker finding fault with capitalism, then offering palliatives, such as limited employee governance of the workplace, that at first sound radical, then prove to be superficial. It is only when Beatty gets to such works as *The Practice of Management* (1954) that we begin to glimpse "the one great thinker management theory has produced." Yet Beatty undercuts his own assertions of the man's profundity: Drucker is "a glib failure," "Panglossian," a peddler of "threadbare" nostrums. Huh? When it comes to admirers like this, 200 pages of text may suit Drucker just fine.

BY HARDY GREEN



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Arcstar is NTT Group's recently launched global end-to-end communications service, which utilizes a high-speed telecommunications highway to connect to major cities across the U.S., Europe and Asia. Arcstar is an essential part of NTT's strategy for global projects, including the Malaysian Multimedia Super Corridor (MSC) and the China-U.S. under sea cable.

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BY STEPHEN H. WILDSTROM

WHAT ABOUT YOUR MILLENNIUM BUG?

Most PC owners have little to worry about, if they take a few precautions

The public has been warned. The year 2000 will hit corporate computers with the force of El Niño, potentially imperiling aircraft, halting tax collections, and generally clobbering commerce. Corporations are spending billions to solve the "Y2K" problem, but what should owners of personal computers do to protect themselves?

In most cases, I think you have little or nothing to worry about. Corporations and governments must fix programs and databases that were designed decades ago. Back then, the millennium was hardly a speck on the horizon, and very high storage costs encouraged programmers to cheat and use just two digits to identify a year. Personal computers entered widespread use in the mid-1980s and were designed with the 21st century in mind. Unfortunately, however, some of the methods for handling the millennium were flawed. These glitches will cause annoyances for some, but they won't threaten your files or the ability of computers to function.

TRICKY ISSUE. The biggest issue is how PCs keep track of the date (Macintoshes don't have Year 2000 problems). The key is a program called the BIOS that is permanently stored in read-only memory and runs when the computer boots up.

The computer's clock puts

out a two-digit year code, and the BIOS adds the century. When the year hits 2000, one of three things will happen, depending on what operating system you are using and what company wrote your computer's BIOS program and when.

If your personal computer



was made after mid-1995, odds are it will handle the date change just fine. Most older computers will show the date as 1900. Once you manually reset the date to 2000, however, the year will be correct from then on, at least until 2099.

Some software will automatically make the correction for you. Windows NT, IBM PC-DOS 7.0, and the upcoming Windows 98 will take note of the change from 1999 to 2000, realize that it is wrong, and fix it. If you run Windows 95, Windows 3.1, or any version of MS-DOS, you can find

shareware programs at repositories such as www.shareware.com that will also deal with the problem—in most cases.

The trouble is that a relatively small number of machines won't respond to either a manual or automatic fix. For example, BIOS chips programmed by Award Software International between April, 1994, and May, 1995, will reset to 1980—the year the IBM PC was introduced—every time the computer is restarted. The only fix is to download a new BIOS program or, in some cases, replace the chips.

How do you find out if you have a problem? Do not set your clock to Dec. 31, 1999, to see what happens.



Year 2000 Resources

GENERAL INFORMATION

- ▶ www.ibm.com/IBM/year2000
- ▶ www.microsoft.com/CIO/Articles/YEAR2000FAQ.htm
- ▶ www.year2000.com

COMPUTER CLOCK

- ▶ www.amibios.com/support/2000.html
- ▶ www.award.com/tech/biosfaqs.htm
- ▶ www.phoenix.com/techsupp/techsupp.html

That just might trigger time bombs in software and cause subscription services to expire. Phoenix Technologies Ltd., a leading writer of BIOS programs, suggests this safe alternative: Start your computer from a floppy containing just the files needed to

boot up. From the command prompt, use the time and date commands to set the clock to a few minutes before midnight on Dec. 31, 1999. Wait until the clock ticks past midnight. Then, without running any other programs, restart the machine and check the date. If it shows Jan. 1, 2000, you're fine. If it doesn't, set the year manually to 2000, and restart again. If the year shows either 1900 or 1980, you probably need a BIOS upgrade. Either way, reset the date and time and reboot.

EXCEL SCHEME. In the corporate world, the nasty Year 2000 woes involve software. Most PC applications are not a problem. Microsoft Corp.'s Excel spreadsheet, for example, stores dates with four-digit years. If you put in a two-digit year, it will assume that years 30 and higher are in the 20th century and years 29 and below are in the 21st. You can override the assumption by entering a four-digit year. Other spreadsheets and databases

programs use similar schemes. Unless you use some poorly designed custom software, you shouldn't have problems.

And even if your computer's date is wrong in the new millennium, you can choose to live with it, if necessary, by setting the system date manually every time you start your computer. You can also choose to ignore wrong dates on your files and electronic mail messages. After all, most of the computers with problems will be at least five years old by 2000. As Bernard Luksic, a Y2K expert at Compaq Computer Corp. puts it: "If you are running an old machine with an old operating system, you may not care."

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BY PAUL CRAIG ROBERTS

WHO DID MORE FOR MANKIND, MOTHER TERESA OR MIKE MILKEN?



GET OVER IT:
Yes, economic growth creates income inequality. It also creates lots of new products and jobs for multitudes

In any country with a market economy, even one forced to bear the burden of a large welfare state, consumers have a wide range of choices for all their wants. People from communist countries who visited America went home in awe of the ability of the market economy to deliver the goods.

Intellectuals, including many academic economists, have a difficult time giving the market its due—despite its unrivaled success. The professor sitting at his desk with his choice of every tobacco for his pipe, every tweed for his back, and every wine and food for his table will nevertheless pen a screed denouncing conspicuous consumption, greed, and income inequality, all of which he will blame on the market.

Economists especially cannot get income inequality out of their system. It galls and perplexes them immensely that the process of wealth creation results in income differences. One recent book, *The Inequality Paradox*, published by the National Policy Assn. with essays by Janet L. Yellen, President Clinton's chief economic adviser, and Robert B. Reich, Clinton's former Labor Secretary, finds inequality to be a disturbing paradox. It blames economic growth for not solving the "problem of income inequality."

Income inequality is not a problem, but a natural consequence of a free society. Nevertheless, judging capitalism by the standards of communism is a favorite pastime for economists. The process allows them to denigrate capitalism for not doing what a different system—a failed and defunct one—was supposed to do but didn't. The market rewards merit, ability, luck, and success with wages, salaries, profits, capital gains, and dividends. The rewards differ because the performances differ. Unequal incomes are proof that the market is doing its job.

STOLEN WEALTH. One day, perhaps, egalitarian ideologues will manipulate genetics to eliminate all distinctions between people, including drive and determination. Then, only luck would account for income differences, and these differences could be eliminated with a "luck tax" that would not harm the incentives of the system.

Intellectuals are unhappy with the market because they don't see wealth as the result of a creative process such as art and literature. Intellectuals view wealth as stolen if made, and mundane if inherited. They think of

wealth as a finite quantity like "exhaustible resources. The people who get rich are the ones who go back for seconds before others get their first helping. Intellectuals simply cannot connect the wealth of a Bill Gates with the creative process.

Not many people have been brave enough to come to the defense of "immoral greed," but ABC-TV's John Stossel recently found one for his program—philosopher David Kelley of the Institute for Objectivist Studies. Kelley calmly noted that Michael R. Milken was a greater benefactor to mankind than Mother Teresa. Milken created wealth, jobs, incomes and new products for large numbers of people, while Mother Teresa redistributed wealth donated by philanthropists. Yet Mother Teresa was praised for her self-sacrifice, and Milken damned for self-interest.

PAYING A PRICE. The attack on "greed" is really an attack on freedom. Among economists it was Milton Friedman more than anyone else who took time from his research to defend economic freedom. The memoirs of Friedman and his wife, Rose, are about to be published by the University of Chicago Press. They show, among many other fascinating things, that economists who had a good word for capitalism in the 1940s, 1950s, 1960s, and 1970s paid a price.

For example, in 1941, not even the determined president and dean of the University of Wisconsin could get Friedman appointed to teaching job over faculty objections. Years later, a person who had studied economics at Duke University in the 1950s later wrote that Friedman at the library in those days had contained nothing by Friedman: "On consulting with my professor, he explained that Duke had a system of screening new material by the appropriate department and the Economics Dept. did not consider your work worthy of carrying." Out of step with the socialist thinking of his time, Friedman was passed over for the Nobel prize for many years. When the award could be avoided no longer and was finally made in 1976, Louis Rukeyser said that if Friedman had been "less committed to human freedom, he would have had his Nobel prize in economics years ago."

Now that communism has failed and its former adherents acknowledge that there is more morality in freedom than in income equality, perhaps American intellectuals also will one day give up communism.

Paul Craig Roberts is a Fellow at the Institute for Political Economy in Washington, D.C., and Research Fellow at The Independent Institute in Oakland, Calif.



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BY GENE KORETZ

INCOME SWINGS CAN BE DEADLY

Health risks for the middle class

With restructuring and contingent employment now purportedly inherent features of modern-day global capitalism, Americans have had to face the possibility that heightened income instability is the price they have to pay for a dynamic, expanding economy. Indeed, most people know folks who lost jobs because of downsizing over the past decade and suffered a sharp (if only temporary) income decline in the process.

A recent study in the *American Journal of Public Health* focuses on an aspect of income instability that has re-

The most provocative findings, however, relate to income stability. The researchers report that sharp income drops—of 50% or more in a five-year period—had little subsequent effect on the already high mortality rates of low-income people. And temporary drops of this size had insignificant effects on the relatively low death rates of high-income (over \$70,000) individuals.

Rather, it was the health of people in the middle income group that suffered significantly if they had experienced a sharp income decline in the prior five years. Such occurrences actually doubled their risk of death, raising it to the elevated levels found among those in the lowest income group.

At the very least, these results are troubling. They confirm that poverty or near-poverty income levels are seriously detrimental to individuals' health, especially when they persist. (Another finding was that low-income people experienced even higher mortality if their low incomes had persisted for at least four of the prior five years.) And they suggest that income instability, even in the form of a temporary sharp drop in income, can pose increased health risks for the middle class.

To the extent that America's rising income inequality and instability will expand the numbers of vulnerable individuals in low- and middle-income groups, write the authors, "the findings forecast a worsening of the nation's health."

SCHOOL IS NOW KINDER TO GIRLS

It's the boys who need pepping up

It has long been thought that girls are at a disadvantage in public schools compared with boys, suffering from lower expectations, less confidence, and often less support from teachers. Whatever the validity of this view in the past, however, a recent nationwide survey of 2,600 high school students and teachers, grades 7 through 12, suggests that it's girls rather than boys who are currently in the ascendancy.

According to the survey, conducted for Metropolitan Life Insurance Co. by Louis Harris & Associates, girls like school more than boys do and have more confidence in their abilities. Some 74% of girls say they are very likely to go to college, compared with just 61% of boys.

Further, more girls than boys feel they get positive feedback from teachers for answering correctly, and more girls

(76% vs. 67%) report getting helpful comments when they answer incorrectly. Similarly, about a third fewer girls than boys (19% vs. 31%) complain that teachers don't listen to them. For their part, teachers see girls as more confident, more focused on education, and more likely to graduate from college.

In many respects, minority girls lead the pack in positive outlook, priding themselves on their ability to succeed and finding their teachers the most encouraging. By contrast, minority boys are the least likely to believe they will attend college or attain their job goals.

Interestingly, these results jibe pretty well with reality. More girls than boys go on to college these days, and minority boys—especially blacks—are the least likely to further their education or do well in the economy.

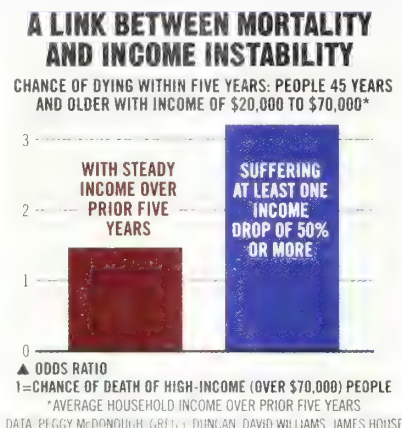
AWAITING ASIA'S EXPORT SURGE

It may be late, but it's coming

Many of the sick Asian economies that were running trade deficits only a little while ago are now running trade surpluses. But the widely forecast tidal wave of Asian exports that will drag the U.S. trade balance far deeper under water hasn't arrived—yet.

The reason, according to economists at Lehman Brothers Inc., is that the recent improvement in Asia's trade performance has been driven by plummeting imports rather than rising exports. Asian imports are being depressed by three powerful forces: currency drops that have dramatically boosted import prices; collapsing domestic demand; and the drying up of credit. Ironically, the latter force is also hampering exports since Asian nations need trade financing to buy the raw materials and intermediate goods that go into exports.

The upshot is that the first hit to America's trade balance, which may already be materializing, will come from falling U.S. exports to the region. The additional powerful blow from surging Asian exports to the U.S. has been temporarily delayed



ceived relatively little attention up to now: its negative impact on individuals' health. The results suggest that sharp income drops can result in significantly higher mortality risks, even when such setbacks are only temporary.

In the study, a team led by Peggy McDonough of Ontario's York University used U.S. survey data from 1972 through 1989 to compare the death rates of people 45 and over with their income levels. As in earlier studies, researchers found that the lower one's income, the higher one's risk of dying.

Other things being equal, those whose household incomes averaged less than \$20,000 (1993 dollars) over a five-year period were two to three times as likely to die in the next five years as those with average incomes over \$70,000. And those with family incomes in a middle range of \$20,000 to \$70,000 had a 50% higher chance of dying than those in the high-income group.

ASIA'S EXPORTS HAVEN'T SURGED—YET



*JAPAN, CHINA, KOREA, TAIWAN, HONG KONG, SINGAPORE, INDONESIA, MALAYSIA, PHILIPPINES
DATA: LEHMAN BROTHERS INC.

JAMES C. COOPER & KATHLEEN MADIGAN

IS THE ECONOMY SLOWING? DON'T BET ON IT JUST YET

The January softness in retailing, housing, and output looks temporary

U.S. ECONOMY Most forecasters expected the economy's feverish pace to cool off last year. By summer, it started to look that way, but by yearend, things sped up again. Now, once again, the forecasters say a slowdown is imminent, partly reflecting expected impact from the Asian crisis. Is the economy really downshifting?

The first-quarter data offer some hints of slower growth, but they are mixed and far from conclusive. Retail sales barely rose in January, but demand in many categories looks as strong as ever. Then in February, first-time jobless claims returned to a very low level, suggesting continued strong labor markets. Also, the key measure of consumer sentiment hit a record, and homebuilders were increasingly upbeat.

Consequently, it's hard to believe that industrial output is gearing down in any big way, if at all. January output was soft, partly because of the mild winter. But amid still-strong demand, December inventories remained lean relative to sales, suggesting little need to trim output on account of excessive stock levels.

U.S. producers are not yet seeing some falloff in exports to Asia. But so far, the Asian effect is showing up mostly in declining import prices (chart). Those competitive pressures are helping back inflation. Producer prices of finished goods fell 0.7% in January, mainly reflecting a big drop in energy prices. Excluding energy and food, the core index dipped 0.1%, and annual core inflation for finished goods was essentially zero.

To be sure, at some point the economy will not be able to maintain the 4% growth it has enjoyed since the summer of 1996. The labor markets are running out of people to hire, and profit growth is already slowing down (page 110). Those factors will eventually erode the strong fundamentals that have kept consumer and capital spending unshakable. Based on the latest data, though, that's not happening yet.

CONSUMERS HOLD THE KEY to any slowdown, since they supply two-thirds of all spending in the economy. That's why January retail sales received so much scrutiny. They rose a scant 0.1%, and the gains for both

November and December were revised downward.

Looking below the headline number, however, sales excluding autos rose a solid 0.5%. Clothing stores posted a 0.7% uptick, restaurant sales increased 0.9%, building materials and hardware stores saw a 1% gain, and department stores enjoyed a 1.5% advance—their best showing in nearly a year. In fact, the main source of weakness came in gasoline sales, more likely a function of price declines than a drop in volume.

First-quarter real consumer spending, calculated in the way it goes into the gross-domestic-product data, appears to be on its way to an annual growth rate of about 3%, little changed from the fourth quarter's 3.2% pace. Unit car sales, which are used in the GDP data, rose to an annual rate of 15.4 million in January, up from the fourth-quarter average of 15 million. Also, the core January components of the retail sales report that go into consumer spending stood well ahead of their fourth-quarter showing.

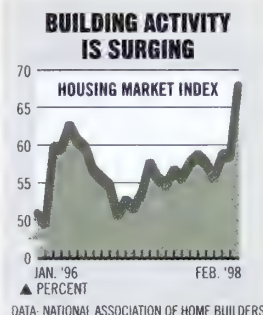
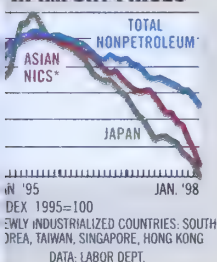
Consumers are also fueling a miniboom in housing. January housing starts dipped 0.3%, but that decline belied a 7% surge in single-family starts. Apartment construction fell sharply, after a big gain in December.

More revealing perhaps is the optimism of builders, based on a monthly survey taken by the National Association of Home Builders. The trade group's housing market index, which tracks both current and expected demand and buyer traffic through model homes, jumped from 59% in January to 68% in February (chart). The February reading was the highest in more than four years, suggesting that low mortgage rates and strong consumer fundamentals will yield a vibrant spring building season.

STRONG DOMESTIC DEMAND is making up for much—but probably not all—of the Asian-based weakness in manufacturers' order books. Industrial production at U.S. factories, mines, and utilities was unchanged from December to January—the first time in 15 months that output failed to grow. But utilities' production plunged 4% amid unusually warm weather.

Manufacturing output alone rose 0.3%, after increasing 0.4% in December, but those gains were only one-

ASIA LEADS THE DROP IN IMPORT PRICES



third of the pace in October and November (chart). Reflecting continued strength in consumer spending and housing, the output of appliances and consumer electronics jumped 3.5% in January, while production of carpeting and furniture rose 2.9%.

Clearly, Asian weakness accounts for some of the softer tone of January production. That's because output of industrial equipment, a big export item to Asia, fell 0.6%, resulting in a rise in business equipment production of only 0.2%, after monthly gains in 1997 averaging 0.8%. Still, output of computer and office gear, most likely headed for U.S. companies, held strong.

Without a considerable slowdown in overall demand, rapid inventory building will not hold back production anytime soon. Inventory growth in 1997 was the fastest in 12 years, but demand was also robust. In December, business inventories rose 0.4%, half as fast as the 0.9% increase in business sales. In the second half of 1997, inventories began to rise faster than sales, but by the end of the year the ratio of inventories to sales, at 1.37 in December, had not risen appreciably.

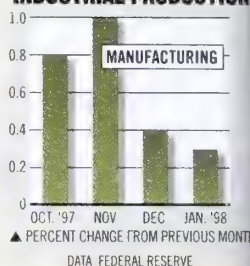
WHILE IMMEDIATE PROSPECTS for U.S. economic growth still look good, one Asian impact is clear: Prices of imports from the region are falling. Excluding oil, import prices dropped 0.6% in January, the largest monthly decline in five years. January decreases were especially large, down 1.2%, for goods

coming from Asia's newly industrializing countries including Hong Kong, Singapore, South Korea, and Taiwan. Prices of Japanese goods fell a steep 1%.

Since the Asian currency crisis began in July, 1997, imported industrial materials and capital equipment have led the price declines, while prices of imported consumer goods have barely fallen, and prices of foreign-made cars have risen. Prices of imported capital goods, however, had been declining at a steep rate even before the crisis began. Prices of imported materials and supplies plunged 1.4% in December and 1.3% in January, suggesting that many businesses are benefiting from cheaper raw materials.

At least for now, the Asian crisis may well be offering more pluses for the economy than minuses, including cheaper commodities to help businesses cope with rising labor costs, lower interest rates that are boosting housing and durable goods, and low inflation generally that is lifting the buying power of household incomes. Indeed, the fallout from Asia has failed to score a direct hit on economic growth so far in 1998. And without such a blow, the U.S. economy could easily gallop right into spring.

A SLOWER PACE FOR INDUSTRIAL PRODUCTION



AUSTRALIA

SO CLOSE TO ASIA, YET SO FAR

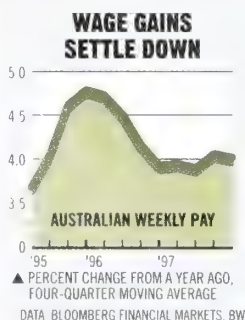
The Reserve Bank of Australia's quarterly report confirmed what had been suspected: The Asian crisis is damaging Australia's trade position, but the domestic economy is still buoyant.

The evidence is in the latest data. In foreign trade, the December deficit was the widest in 2½ years. Imports surged, but exports dropped, particularly shipments to Korea. Tourism was also hit, as the number of Asian visitors fell 23% from last year.

Labor markets, though, are doing well. In January, some 23,100 full-time positions were created. The jobless rate inched up to 8.2%, but that was from the two-year low of 8.1% hit in December.

But that's not to say job prospects are immune to Asia's crisis. A survey found that manufacturers and mining concerns expect to cut payrolls this year because of the export slump, while service industries and construction will boost hiring.

Even with the improvement in job growth, pay gains remain within the RBA's target. In the fourth quarter, weekly pay was up 3.7% from a year ago, down from the third quarter's 4.4% increase (chart). But pay and jobs are rising fast enough to keep consumers upbeat, and that optimism is benefiting housing. Home-loan approvals rose 1.3% in December, while housing permits



were up 0.8% in December, the third monthly increase in a row. Strength from domestic sources should enable the Australian economy to grow 4% in 1998, despite the fallout from Asia. The economy probably expanded by about 3.1% in 1997.

With wage growth unlikely to reignite domestic inflation, the RBA is not expected to raise interest rates soon. That prospect is depressing the already weak Australian dollar. In the past six months, the "Aussie" has fallen 11% against the U.S. greenback and 3% against the yen. Asian worries are also hurting the stock market as investors gamble that falling exports will crimp earnings. In fact, if exports fall more than anticipated, the next move by the RBA could be a rate cut to keep domestic demand going.

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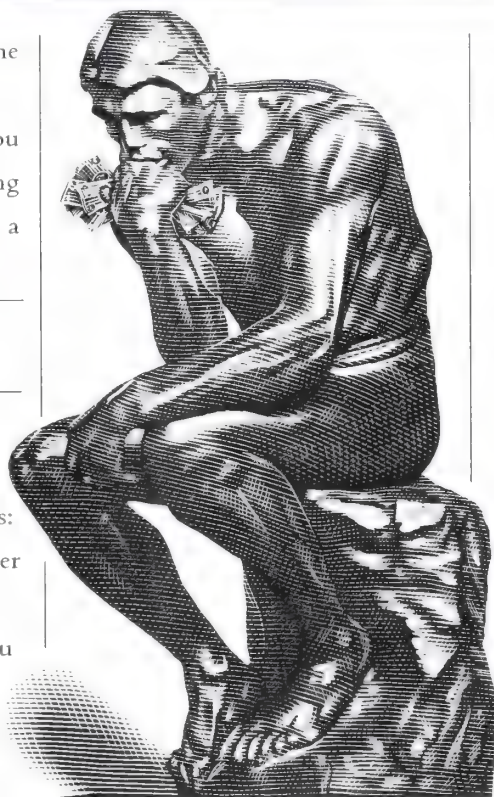
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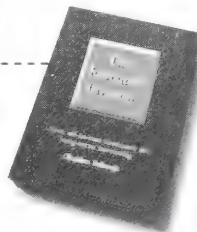


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The Way It Should Be.

INVASION OF THE BARGAIN SNATCHERS

Asia's cash crisis is sparking a frenzy of mergers and acquisitions

Asia had never been a priority for Prince Alwaleed bin Talal. The Saudi investor, who has accumulated a net worth of \$11 billion in deals from New York to Beirut, considered dozens of potential investments in Asia over the years, but he always balked. "Valuations were just too high," he says. "It was crazy."

That was then. Now, the Prince is jetting across Asia in his cream-colored Boeing 727, collecting bargains. In the past three months, Alwaleed has picked up stakes in Singapore property group HPL, Malaysian auto maker Proton, and South Korea's Daewoo—and he's looking for more. "When Asia comes back, and it will, it's going to be even stronger than it was before this crisis," predicts Alwaleed.

As Asia's debt crisis takes a growing toll on cash-strapped companies and governments, longstanding barriers to cross-border mergers and acquisitions are starting to crumble. From Tokyo to Seoul to Jakarta, Western investors—from multinationals to opportunistic vulture funds—are joining the Prince in the business-buying bazaar.

There is a wealth of merchandise to

choose from. South Korea's Samsung, Indonesia's Salim, and Thailand's Charoen Pokphand are among the powerful business groups trying to sell subsidiaries in industries such as cars, chemicals, and finance. "For years, everything these groups touched turned to gold," says Hong Kong merchant banker Tony Miller, a general partner of Asian Investment

Partners. "Now, that gold is turning to dross."

So far, the sums involved are relatively small. The estimated \$52 billion in deals done in all of East Asia in 1997, according to *M&A Asia*, accounted for about 3% of all deals worldwide. But the amount is expected to mushroom. A recent survey of U.S. and European multi-



inals by consultant Renaissance nomic found that 64% planned to up acquisition activities in the re- "We are pleasantly surprised with quality and quantity of opportunities have emerged," says Peter N. as, group vice-president of Clorox which is in talks with several possibilities.

eing some of their most ambitious res sold off may be a humbling rience for East Asians. But when restructuring is complete, the realization of overbuilt industries the influx of foreign capital (d put the region on firmer foot- That's especially important in the ce sector, where many of the s are now taking place. East s commercial banks must raise at \$260 billion in new capital to back on their feet, estimates J. P. gan Securities Asia Ltd. banking 7st John Wadle. Industries such etrochemicals, autos, and prop- development need similar help. **ING HAND.** For American com- s, the opportunities are breath- ing. Asia's crisis gives them a ce to grab strategic ground—on own terms—in economies still cted to be among the world's est growth markets in the 21st ury. "The whole area is going to nd in the next decades," says l Motor Co. Chairman Alexan- I. Trotman. "We plan to be part at." Ford is targeting 10% of Asian market by 2005, from less 1% now.

ith a nudge from the Interna- l Monetary Fund, more oppor- ies may soon be available. The s pushing an overhaul of invest- rules in Korea, Indonesia, and land as a condition of financial and that should make broad re- turning less difficult.

at's the upside. The downside e risk that accompanies such ing. Many of the Asian companies can be acquired have weak man- nent, Byzantine cross-holdings, murky financial record-keeping. latest headlines—riots in In- sia, President Suharto's dismissal e head of the central bank, and l defaults by Thai companies—are nders that this region is not for the e-hearted.

one of this has discouraged deal- ers, though. Gary Stead, Merrill h & Co.'s Singapore-based managing tor in charge of Asian mergers and isitions, has upped his team from 3 bankers and is still recruiting. Hong

Kong-based merchant bank Jardine Fleming Securities Ltd., the leading M&A house in the region in 1997, expects merger activity to account for about 75% of corporate-finance earnings in 1998, vs. about 30% last year.

Korea's cash-strapped *chaebol* have been the most aggressive in flogging as- sets. Coca-Cola Co. and Procter & Gamble Co. have picked up big bottling and

THE DEALS ARE PILING UP...

YAMAICHI SECURITIES

Merrill Lynch is spending \$300 million to buy portions of Yamaichi's Japan brokerage business to get critical mass in Japan fast.

CEPA

Southern Co. of the U.S. has bought control of this Hong Kong power-plant operator for \$2.1 billion. Managing it has been tough.

RENAISSANCE HOTELS

This division of Hong Kong's New World Group has gone to Marriott for \$1 billion.

DOOSAN GROUP

This Korean *chaebol* has sold its bottling unit to Coca-Cola of the U.S. for \$432 million.

PACIFIC LINK COMMUNICATIONS

Hong Kong Telecom has bought this cellular franchise for \$350 million.

...AND MORE ARE COMING

HAN WHA REFINERY

Korea's Han Wha Corp. wants to raise cash by selling this unit for an estimated \$2.2 billion.

INTERCONTINENTAL HOTELS

Japan's hard-pressed Saison Group might raise as much as \$3 billion by selling this chain of high-class hotels.

HAGEMEYER

Conglomerate First Pacific of Hong Kong is ready to sell this Amsterdam-based trading group for \$1.8 billion.

ASIANA AIRLINES

Korea's Kumho Group is willing to part with 50% of this airline, which, for now, is a money-loser.

DATA: BUSINESS WEEK, M&A ASIA

paper operations from troubled *chaebol*. Han Wha Corp., formerly Korea Explosives Group, has sold small operations to Alliance Capital Management and Japan's NSK Ltd., and buyers are now eyeing its crown jewel: an oil refinery valued at \$2.2 billion. Daesang Group is talking to Cargill and Tyson Foods as part of its drive to unload businesses

worth \$1 billion. "The *chaebol* have tried to avoid downsizing," says Park Kyung Min, chief investment officer at Asset Korea Capital Management. "But they have no choice."

The biggest deals could involve the carmaking *chaebol*. Six years after a bitter corporate divorce, General Motors Corp. is in talks with Daewoo Motors. And Ford began talks in mid-February with Samsung, whose \$1.6 billion stake in a new auto plant is threatening to hobble the entire group. If the two companies strike a deal, analysts speculate, the joint venture could then try to buy the 83% of Kia Motors Corp. that Ford does not yet own.

FINANCE BLITZ. Across the rest of Asia, the most profound impact will likely be felt in financial services. Many buyers are still window shopping. But Banque Nationale de Paris has bought the China corporate-finance business of Peregrine Investments Holdings Ltd., while Prudential Securities Inc. picked up Thai broker Nava Securities. GE Capital Services Inc. is pumping \$575 million into a joint venture with ailing Toho Mutual Life Insurance Co. And on Feb. 12, Merrill scooped up 30 branch offices, with 2,000 employees, from bankrupt Yamaichi Securities. Says President Herbert M. Allison Jr.: "Merrill Lynch is bullish about Japan."

Real estate is also getting snapped up. Regent Pacific Group Ltd., a Hong Kong-based mutual-fund house, has bought 500 new Jakarta apartments for 10% to 15% of their price before Asia's troubles began, says Managing Director James Mellon.

Westerners aren't the only ones buying. Hong Kong's First Pacific Co. sold its faltering cellular division to Hong Kong Telecom for \$350 million. And Singapore's DBS Bank is buying Thailand's 12th-largest bank, Thai Danu Bank Public, and the Philippines' Bank of Southeast Asia.

The reshaping of Corporate Asia won't happen overnight. Much will depend on the success of the IMF rescue and reforms. And, with cross-border M&A so new to Asia, there may be a period of adjustment in these marriages. But the takeovers will help governments and companies alike. The ground is being laid for restructuring on a grander scale than ever before seen in this region.

By Mark L. Clifford in Hong Kong, with Moon Ihwan in Seoul, Keith Naughton in Detroit, John Rossant in Rome, and Pete Engardio in New York



WASHINGTON

THE GOP SQUABBLES, AND BUSINESS SUFFERS

Republican split means the corporate agenda gets short shrift

Just a few weeks ago, the political landscape in Washington looked pretty good to Corporate America. After all, there were prospects of a budget surplus—and perhaps tax cuts. Labor lobbyists were distracted by union corruption scandals. And congressional Republicans—flush with big-bucks donations from business—seemed to have a lock on Congress next fall.

So why all the long faces along the K Street Corridor? Business lobbyists are coming to the conclusion that the 1998 session will not only be unproductive, but potentially bad for business.

For starters, priorities such as fast-track trade negotiating authority for the President, corporate tax cuts, and sweeping tort reform (page 53) appear dead. Worse, corporate coalitions are

losing the battle against popular White House proposals that will hit them directly in the pocket: a higher federal minimum wage and a patient “bill of rights” for members of managed-care plans. To the Republicans’ dismay, the President’s popularity is soaring, and support for his programs—not their tax breaks—is rising as well. He is, laments U.S. Chamber of Commerce President Thomas J. Donohue, “the best politician in my lifetime.”

LONG FEUD. On the other hand, the GOP is too disorganized to mount an effective counterattack. “The reality is that the Republican majority is struggling,” gripes a veteran business rep. “There’s no unifying vision.” House Speaker Newt Gingrich (R-Ga.) continues to preside over an unruly caucus of feuding

conservatives and moderates. And Senate Majority Leader Trent Lott (R-Miss.) hasn’t galvanized his forces.

Republicans can blame the loss of one top priority—getting fast-track trade authorization—on pro-labor Democrats. But on many other issues, it is their own fighting that’s stalling legislation. The effort to get additional U.S. funding for the International Monetary Fund to help in East Asia. GOP abortion foes vow to sink the \$10 billion IMF package unless Congress cuts off funds to international groups that counsel about or perform abortions. Other GOP hard-liners want tough conditions on any money lent to Asian economies.

Even when business and Hill leaders agree—such as on tax cuts—lobbyists find business interests low on the party’s priority list. With an election looming, Republicans are focusing on middle-class voters with such goodies as a reduced “marriage penalty” for two-earner families. Big capital-gains cuts or corporate breaks seem unlikely, though small business may win estate tax relief.

The Democrats, meanwhile, are dithering their own election-year good before voters. Clinton and Senator Edward M. Kennedy (D-Mass.) are leading a push to raise the minimum wage at least \$1 an hour over two years. Business leaders say the hike will mean fewer jobs, but they know they’ll have trouble stopping some allies in the Congress from backing a proposal with wide public support. Congress has never voted down an increase in the minimum wage, and with the economy still expanding, it’s unlikely it will do so this year.

Business may have to accept other potentially costly voter-friendly programs such as expanded child-care services, too. Many Hill Republicans have jumped on President Clinton’s day-care

A BAD SESSION FOR BUSINESS

WHAT BUSINESS WANTS—BUT IS UNLIKELY TO GET

REVIVAL OF FAST-TRACK TRADE LEGISLATION A top priority for many in Corporate America, but Democratic resistance makes it a nonstarter.

TAX CUTS Corporate tax breaks are low on the priority list of Hill Republicans; estate-tax relief for small business is possible.

IMF FUNDING Business is concerned that \$18 billion to compensate the IMF for its Asia rescue may fall victim to anti-abortion Republicans who insist international family-planning assistance be eliminated first.

WHAT BUSINESS MIGHT GET—BUT DOESN'T REALLY WANT

MINIMUM WAGE HIKE Congress is under intense pressure to give low-wage workers a share in the economic boom.

FAMILY MANDATES Republican leaders may not be able to withstand pressure to pass child-care legislation or to extend the Family & Medical Leave Act to smaller businesses.

PATIENT BILL OF RIGHTS The insurance industry and small-business groups oppose legislation to protect the rights of managed-care patients. But even lobbyists admit this idea has legs.

dwagon—even upping the ante with ax break for stay-at-home moms in lition to incentives for business. Then there's the backlash against os. The White House and a bloc of gressional Republicans have proposed ew set of guarantees for patients, h as the right to medical specialists l information about treatments. Re- licans are sympathetic to business cerns about how the plan would raise ts, but many don't want to be on wrong side of the issue with voters.

Among the leading advocates of reform are Senator Alfonse M. D'Amato (R-N.Y.), who faces a tough reelection battle in 1998, and Representative Charlie Norwood (R-Ga.) "They don't think they can be seen neglecting patients," concedes Thomas A. Scully, president of the Federation of American Health Systems, representing for-profit hospitals.

Some corporate lobbyists say they understand why the GOP would rather shun controversy than do battle for them. With Republicans hoping to main-

tain their majorities in the House and Senate, "they don't want to do anything to rock the boat," says one lobbyist. "That means don't get into any nasty fights with Clinton."

If that's what it takes to keep Capitol Hill in GOP hands, execs are willing to put up with some disappointments this session. They figure 1998 may be a bust, but there's always next year.

By Richard S. Dunham, with Mike McNamee and Howard Gleckman, in Washington

COMMENTARY

By Richard S. Dunham and Stan Crock

WHY AN IRAQ ATTACK OFFERS NO RELIEF FOR CLINTON

It's a truism of American politics: When a President gets in a jam, he often retreats to the foreign policy arena, hoping to return a conquering hero. But Bill Clinton is turning that axiom on its head.

Clinton's popular domestic-policy agenda has resuscitated his job-approval ratings in the wake of allegations that he had an affair with former White House intern Monica S. Lewinsky. But the President's charmed life seems to end at the water's edge. As he heads for a military showdown with Iraqi President Saddam Hussein, Clinton is faltering in his campaign to keep unqualified congressional support and get the American people behind him. A mid-February Gallup Poll shows only 41% of the public favors an assault on Iraq, a decline of nine points in two weeks.

WAVERING SUPPORT. Clearly, Clinton would rather be talking about child care. "There's nothing he relishes like the domestic issues," says Brent Scowcroft, George Bush's National Security Adviser. "I still don't think he's interested in foreign policy."

As Clinton agreed to let U.N. Secretary General Kofi Annan make a last-minute diplomatic mission to Baghdad on Feb. 20, congressional Republicans have sensed White House weakness. No longer willing to mute their criticism, GOP leaders have begun blasting Clinton and his national security team for an incoherent policy. Senator John McCain (R-Ariz.) scold-



ed the President for having no short-term plan to cripple the Iraqi strongman's power bases and no long-term strategy to undermine his regime.

Even Democrats are second-guessing Clinton's game plan. Former President Jimmy Carter says an attack would be counterproductive and make Saddam "a hero" to Arabs.

With public and Capitol Hill support wavering, the White House launched a marketing campaign on Feb. 17 with a Presidential speech at the Pentagon. One day later, Defense Secretary William S. Cohen, Secretary of State Madeleine K. Albright, and National Security Adviser Samuel R. Berger all attended a televised town hall meeting at Ohio State University. But the event backfired; the trio was hooted and jeered. Republicans lost no time declaring it a public

relations disaster.

But even a successful town meeting wouldn't compensate for a flawed policy toward Iraq. The Clintonites claim their goal is to limit Saddam's capability to produce chemical and biological weapons, but they admit that even a massive bombing raid won't eliminate the weapons entirely.

And they don't have an alternate strategy to push out Saddam, either. Attempts to strengthen Saddam's enemies, meanwhile, have been hampered by factionalism among Iraq's Kurdish rebels. And a clandestine U.S. operation to topple him appears to have been halted. The Administration "thrashes around, but isn't solving anything," says Kenneth M. Pollack of the Washington Institute for Near East Policy.

With no easy options for dealing with Saddam, it's little wonder that the President seemed ill at ease during his Pentagon appearance. Cynics charge he's merely adopting a *Wag the Dog* strategy—creating a foreign flap to distract attention from a sex scandal. But the truth is, this President is better off picking fights with Republicans over the minimum wage than battling foreign dictators over U.N. inspections. Not only is he more comfortable, but victory is more likely.

Dunham covers the White House, and Crock covers the State Dept.

WEAK TEAM?

Clinton with his foreign policy advisers: (from left) Berger, Cohen, Richard-son, and Albright

THE FED

GREENSPAN'S BATTLE AGAINST OLD DOGMA

The Fed is torn: Inflation hawks want a rate hike now

Given the mounting evidence of a productivity surge, you might think Federal Reserve Chairman Alan Greenspan would have convinced Fed colleagues by now that the U.S. economy can grow faster than 2% without risking a new burst of inflation.

But the traditionalists can be a hard group to turn around. Despite recent figures showing productivity gains running at nearly double the trend rate since the 1970s, many Fed officials still believe that robust growth and tight labor markets are sure to trigger an upsurge in prices. So the battle within the Fed continues: Greenspan wants to stand pat on rates until he sees signs of inflation, while the hawks want to hike rates because they believe the productivity gains won't last and that rapid growth will inevitably lead to inflation.

The latest evidence of this split: newly released minutes of the Dec. 16 meeting of the Federal Open Market Committee (FOMC). They show that several officials were reluctant to follow Greenspan—who advocated dropping the Fed's bias toward raising rates.

SHARP DIVISION. The chairman put forward a neutral view on rates, arguing that Asia's economic crisis would slow the U.S. economy. Although the FOMC ultimately voted with Greenspan, some members seemed allied philosophically with Richmond Reserve Bank President J. Alfred Broaddus Jr. He favored an immediate rate hike, arguing that "persisting strength in aggregate demand" could spark inflation. David M. Jones, chief economist at Aubrey G. Lanston & Co., a longtime Fed watcher, notes that there is clearly a sharp division on the FOMC. "My sense is the majority didn't want to change the bias

[in December] because they think the next move is to tighten. But Greenspan is out front, pulling everyone along."

The FOMC took a pass on a rate hike when it met again on Feb. 3-4. But restive policymakers may not wait much longer. The growth-phobes argue that with demand still strong and unemployment at 4.7%, businesses are starting

This bolsters Greenspan's argument with the hard-liners. Productivity gains are lowering unit labor costs so that employers can pay higher wages and still turn profits—despite their inability to raise prices. In the manufacturing sector, unit labor costs actually fell 0.1% last year, despite a 3.5% boost in hourly pay. "The new era is here, and we're just at the tip of the iceberg," says John Wesbury, chief economist at GRI. Kubik, Stephens & Thompson Inc., a Chicago investment firm. "Over the next year or two, we're going to be surprised by the upside in productivity."

"FAILING." A few Fed members may be coming around. At least they're questioning old dogma, including the ingrained relationship between low un-

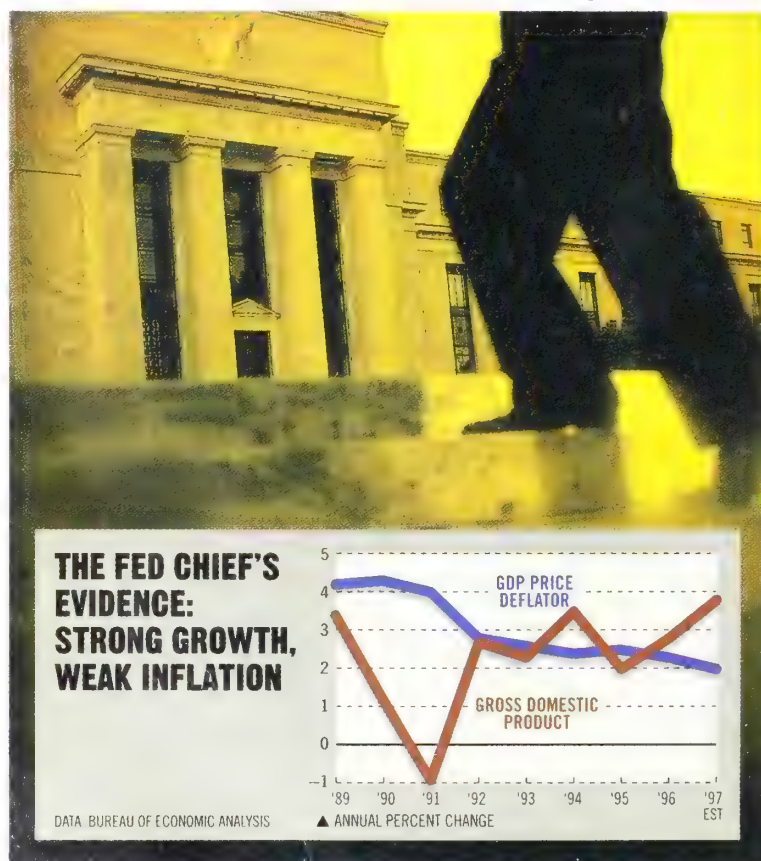
employment and rising inflation. "A lot of the old models we've been using are failing," admits Arthur J. Rolnick, research director for the Minneapolis Federal Reserve. "These models of demand-driven and demand-side changes such as technological advances

Meanwhile, Greenspan tells them that even now the real productivity gains are understated. He distrusts published data so much that he makes his research staffers construct a second index. Their charge is to "zero out" even the service industry that shows falling productivity, such as health care, and recalculate an average. The reason: Greenspan doesn't believe it's possible in today's super-competitive climate that an industry can become less efficient.

But Greenspan is making few converts on the FOMC. Traditionalists argue that it's easy to show short-run productivity gains when demand is so hot. But if growth slows, productivity will collapse. "I do not see clear evidence of a break in the productivity trend," Fed Governor Lawrence H. Meyer said recently.

Such convictions illustrate just how much missionary work remains for Greenspan to do. But if the productivity statistics stay strong, he will find it easier to prevail.

By Dean Foust in Washington



to bid up wages to attract new workers.

Since the meeting, the strong 1997 productivity numbers have rolled in—accompanied by a sharp upward revision in the 1996 figure. Coming off of a 3.6% gain in the third quarter, nonfarm productivity rose at an impressive 2.0% annual rate between October and December—nearly three times what Wall Street economists expected. Then, on Feb. 18, the Labor Dept. reported that the producer price index dropped by 0.7% in January, continuing a downward trend that began in 1997.



"We had trouble telling the Americans that we had the right to investigate.... But it's normal that we look into the effects of a merger on a market."

KAREL VAN MIERT
Competition Commissioner

TRUSTBUSTERS

THE REGULATORY MUSCLES FROM BRUSSELS

The EC's Van Miert has earned respect as a tough negotiator

It was a blunt warning. European Competition Commissioner Karel Van Miert was testifying to the European Parliament on Feb. 5 about the proposed merger of the world's second-largest accounting firm, Ernst & Young, with KPMG Peat Marwick, its closest rival. The combined firm would have had 40% of the European market and 36% of the market worldwide, and Van Miert was concerned that the firms' clients would not be left with enough choices of auditors. "We received several complaints" from customers, Van Miert says. "There were large problems we had to investigate."

The Commission agreed to launch a five-month investigation—and that was enough for Ernst & Young to scuttle the planned megamerger. The giant auditing firms are in good company: These days, some of the biggest U.S. corporations are finding the EC a surprising roadblock to global consolidation plans. **IN CLUB.** Manning the barricade is Van Miert, the top trustbuster in Brussels. He has held up the long-attempted takeover between British Airways and American Airlines, and he's now looking at links between KLM Royal Dutch Airlines and Northwest Airlines, Lufthansa and United Airlines Inc., and the agreement among Delta Air Lines, Austrian Airlines, Sabena, and Swissair. He's also reviewing the planned Price Waterhouse-

Coopers & Lybrand merger. Last summer, the 55-year-old Van Miert succeeded in forcing Boeing to give up its exclusive 20-year deals with airlines to win approval for its merger with McDonnell Douglas Corp. "We had trouble telling the Americans that we had the right to investigate" that case, says Van Miert. "But it's normal that we look into the effects of a merger on a market."

Surprisingly, the activist antitrust chief has a number of fans in Corporate America. "Instead of having to go to half a dozen or more different antitrust reviews in every European country, more and more companies can get by with only one," says David Chijner, an antitrust specialist at the New York-based law firm Weil, Gotshal & Manges. "And the reviews generally are quick and efficient." Van Miert's crusade to open up markets such as telecom, aviation, and energy also has earned him fans at companies such as Enron and Ameritech. "Van Miert is the most pro-competition person in Brussels, opening up all sorts of opportunities for American business," says David Burnett, an economic officer at the American Mission to the European Union.

That's quite an accomplishment for a Belgian farmer's son who made his name as chairman of the Flemish socialist party. Van Miert joined the EC as transportation commissioner in 1989, and when he took over the antitrust portfolio in 1993, expectations were low. "People didn't expect this socialist to be a vigorous free-marketeer," says Alexandre Mencik, a partner at Squire, Sanders & Dempsey in Brussels.

But Van Miert had gradually developed an aversion to monopolies. "When I was involved in Belgian politics, I was a privileged witness to the dangers of monopolies," he says. He became fed up, he says, with the high prices and poor service of Belgium's airline, Sabena, and Belgacom, its telephone company.

Van Miert began deregulating airlines as transportation commissioner and is still on the case. "Airlines are one of our most sensitive areas," he says. His reach now extends to industries from

Deal-Busting Scorecard

BOEING-McDONNELL DOUGLAS

Forced Boeing to give up its exclusive deals with airlines to win approval for the merger.

BRITISH AIRWAYS-AMERICAN AIRLINES

For more than 18 months, Van Miert has held up the planned deal, insisting that BA give away slots at London's Heathrow Airport to give low-fare startups a leg up. Also looking at other airline deals.

ERNST & YOUNG-KPMG PEAT MARWICK

After Van Miert voiced his concerns and launched a five-month probe of the planned merger, Ernst & Young called off the deal.

KIRCH-BERTELSMANN

Van Miert is planning to block the German companies' planned digital-TV deal, a move that could benefit Hollywood.

PRICE WATERHOUSE-COOPERS & LYBRAND

Van Miert is reviewing the deal. While he may go easy with the KPMG-Ernst & Young deal off, others predict he may be tough after his success on the other accounting merger.

European soccer to ice cream manufacturers.

When the KPMG-Ernst & Young deal was proposed last October, Van Miert was immediately skeptical and put his troops to work evaluating the deal. "They asked our clients what they thought of the plan, and they asked us what our profits were on individual audits," complains Jan De Dekker, a partner at Ernst & Young's Brussels office. Ultimately, Ernst & Young deep-sixed the plan. "The likelihood of regulatory approval was dimming," says Philip Laskawy, Ernst's chairman.

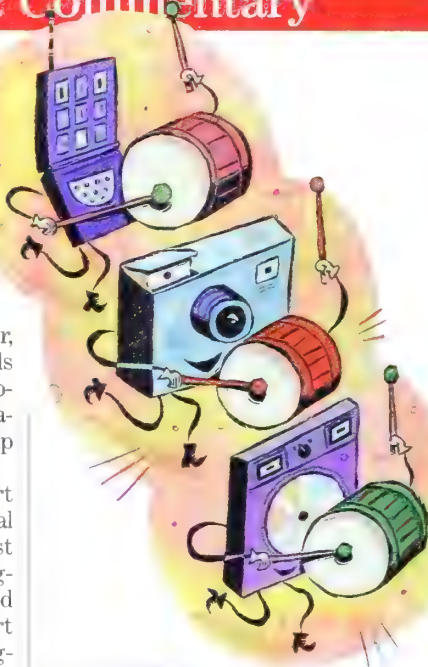
HEAVY HAND? Critics say Van Miert sometimes blocks deals more for political than competitive reasons. During last summer's dogfight over the Boeing-McDonnell Douglas merger, some said he was mainly fighting to support Europe's Airbus Industrie. "Boeing-McDonnell Douglas represents a grave threat to Airbus, which represents just about the only real pan-European success story," says Weil, Gotshal's Chijner.

Some airlines see a heavy hand in Van Miert's approach to the British Airways alliance with American Airlines, which he has held up for more than 18 months. Van Miert insists that BA give away slots at London's Heathrow Airport to make way for low-fare startups. "This slot war has nothing to do with antitrust law and everything with politics and interventionism," argues Stephen Kinsella of the British law firm Herbert Smith. But Van Miert says that in both the Boeing and BA deals, he simply has been making sure dominant players cannot become monopolists.

The antitrust chief says he has already improved transatlantic antitrust cooperation. For example, he joined the U.S. in forcing Microsoft Corp. to commit to a consent decree in 1995 and is backing the Justice Dept.'s increasingly aggressive look at the company. And he is preparing to stop a German digital-TV deal between broadcasters Bertelsmann and Kirch that would lock up the German TV market. "That will help Hollywood," says the American Mission's Burnett.

Van Miert, whose term expires at the end of 1999, has been mentioned as a potential candidate for EC president. But he insists that his next move is out to pasture—literally. "I would like to return to my farm and do some more gardening," he says. Still, after shaking up businesses on both sides of the Atlantic, it's hard to imagine Van Miert back on the farm.

By William Echikson in Brussels, with Larry Light in New York



MARKETING

DURACELL'S BUNNY BUSTER?

The battery maker says its new Ultra trounces rivals

In today's ever more mobile society, it sometimes seems as if everything—from your child's power-assisted lollipop to the latest palmtop—eats batteries. Yet we don't have much choice in disposable batteries: Despite constant battles between the Energizer Bunny and Duracell International's Copper Top, tests have shown there isn't much difference between battery brands—they all poop out at about the same rate.

But now Duracell says it has shattered the stalemate. On Feb. 18, it unveiled Duracell Ultra, a new line of AA and AAA alkaline batteries specifically designed for power-draining digital cameras, cell phones, and remote-controlled toys. Duracell claims the Ultra, in development for four years, will last up to 50% longer than ordinary alkaline batteries in such devices. Duracell squeezed more performance out of the alkaline design by reducing electrical resistance and reformulating the battery's chemistry, company officials say. Duracell will start shipping the Ultra in May and plans to ask a 20% premium over its existing batteries, or about \$5 for a four-pack of AAs. Part of the marketing plan is to convince

rechargeable battery users to switch alkaline disposables for the convenience.

Other battery makers have tweaked batteries for high-tech products. Eastman Kodak, No. 4 in batteries, says its new Photolife AAs outlast the competition in its digital cameras. And No. 2 Energizer has been promoting its new AA AAA batteries as superior for "high-drain devices" like cell phones and minidisc players. It maintains they are superior even to the Ultra. But the new Ultra "a wake-up call for Energizer," says Jeffrey Hill, managing director of the Meridian Consulting Group in Westport, Conn. **GILLETTE'S EDGE.** Experts expect Duracell to have a fairly easy time upgrading users to the Ultra. Gillette Co., which bought Duracell in 1996, has a long record of convincing consumers to pay more for the next thing in shaving. And with the Ultra, "a 20% premium seems a small price to pay for the convenience of a 50% improvement," says Suzanne Hogan, senior partner at Lippincott Margulies Inc. Duracell believes Ultra can capture 10% of the \$3 billion North American and European market for AA and AAA batteries, boosting its market share by 3%, to 51%.

Duracell is also betting the Ultra will make alkaline batteries more attractive to users of cell phones and camcorders. The company estimates that just 8% of cell phones now accept alkaline batteries. Duracell will now be able to make a stronger case that "an alkaline battery is a better choice" for users like so-called safety subscribers, who have cell phones mainly for emergencies, says Brian Barnett, director of battery industry studies for Arthur D. Little Inc. The reason: While rechargeables lose their charge over time, alkaline holds its for years.

Already, Duracell has helped convince

"A 20% premium seems a small price to pay for the convenience of a 50% improvement"

Philips Electronics and Alcatel Alsthom to launch cell phones with a built-in alkaline option, and Sony to offer Handycam with that capability. And "we now have design projects under way with 50 other manufacturers," says Peter Hoffman, Duracell's President of commercial operations.

Given the fierce battery wars, competitors will doubtless come up with similar products. But for now, the Copper Top has the bunny on the run.

By William C. Symonds in Boston

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COMMENTARY

By John Carey

DON'T BAN CLONING. DON'T BAN CLONING

Judging from the frenzy in Congress and state assemblies across the country, you'd think the cloning of people poses a greater threat to humanity than Saddam Hussein. Seven bills to ban the creation of duplicate humans have been

introduced on Capitol Hill since Dolly the sheep was cloned in Britain a year and a half ago. Thirty-six similar bills are pending in 24 state legislatures, and California has already passed one.

No question, creating people by copying someone's genes is deeply offensive to many. As Ronald Cole-Turner of the Pittsburgh Theological Seminary argues, "cloning would be an insult to the dignity of human life as creatures in the image of God."

But whatever one's religious views, this rush to ban cloning is distressingly ill-conceived. Many of the proposed restrictions could cripple important research. The most egregious ex-

ample: a measure introduced in Florida last year to ban the cloning of all human cells. Since cloning cells is crucial for biomedical research, the bill would have prevented experiments on everything from the AIDS virus to the genes that cause cancer. The bill has since been toned down.

BAD SEED? Fact is, new restrictions aren't necessary. The Food & Drug Administration already has the power to quash attempts to clone people. Eccentric scientists such as Chicago-area physicist and fertility researcher Richard Seed can announce plans to open human-cloning clinics. But without FDA approval, they'll be committing a crime. And they won't get FDA approval: The chances of producing a normal, healthy human by cloning are still far too slim for the agency—or any responsible scientist—to permit it. "There's no threat from Dr.

Richard Seed right now," says Carl B. Feldbaum, president of the Biotechnology Industry Organization.

To their credit, congressional backers of cloning bans are trying to minimize the effect on research. Representative Vernon J. Ehlers (R-Mich.),

for instance, is sponsoring a measure that specifically permits cloning plants, animals, and virtually every non-human type of cell. With some lawmakers calling for far more draconian measures, "I thought I was doing industry a favor," says Ehlers. "My bill provides protection for 99.99% of the research they want to do."

But his bill could be more harmful than that. It essentially prohibits the use of any cell from a person to create a clone. Yet a hugely promising area of research involves growing new cells to replace, say, damaged pancreases in diabetics. And one approach to creating these cells is to transfer

the nucleus from a human cell into an egg. The resulting embryo—a clone—could then be tweaked to grow into any type of cell.

This process in itself is wildly controversial. At the heart of the issue, says Dolly creator Ian Wilmut of the Roslin Institute in Scotland, is the question: "Is it right to produce an embryo as a source of cells?" Many scientists and doctors say yes. But abortion foes, who have won bans on

any federal funding for human-embryo research, are appalled. And their opposition explains why any cloning ban Congress passes likely will slam the door on this type of research.

That would be a mistake. "What's

at stake here are life-saving technologies, the only hope for thousands afflicted with Parkinson's disease, diabetes, cancer, and other deadly and disabling diseases," argues Origen Therapeutics Inc. Chairman Michael D. West. This is an exaggeration, of course, but West's comments do contain a big nugget of truth.

QUICK FIX. Congress' best course of action? Do nothing. If gaps appear in the FDA's authority, lawmakers could enact a quick fix. Or if they have to take a stand now, they could pass a bill like the one proposed by Senators Edward M. Kennedy (D-Mass.) and Dianne Feinstein (D-Calif.). It would bar implantation of an embryo

clone into a woman's womb, preventing the birth of a cloned child but not thwarting a promising technology. Further, the ban would be reevaluated in 5 and 10 years, giving scientists and lawmakers a chance to reconsider the law in light of new research.

Religious fervor aside, whether cloning is morally acceptable boils down to one simple question. As Arthur L. Caplan, director of the Center for Bioethics at the University of Pennsylvania, puts it: "Is it really in the interests of a person to be made in someone else's image?"

The answer may be no. But better to explore these ideas than to close the door prematurely on cloning—and run the risk of curbing enormously promising research.

Carey covers science issues from Washington.

An outright ban on duplication of human cells would scuttle promising research



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TRANSPORTATION

A DESPERATE EFFORT TO CLEAR THE TRACKS

If Union Pacific's latest brainstorm falters, it may lose lines

Thanks to a deal cut on Feb. 12 with rival Burlington Northern Santa Fe Corp., Union Pacific Chief Executive Richard K. Davidson has some breathing room. The deal sidetracks—for the moment—efforts to rearrange his company's 1996 merger with Southern Pacific Rail Corp. Since last summer, difficulties in merging UP and SP operations have led to massive freight delays. The pact, a major concession by Davidson, calls for BNSF and Union Pacific Corp. to share ownership of a rail line between Houston and New Orleans, which should help unsnarl traffic around the Gulf Coast.

It also should keep regulators at bay. Burlington Northern had been threatening to ask the Surface Transportation Board to review the UP-SP merger unless some joint-operating arrangement could be worked out. And on Feb. 17 the STB nixed a request by the Texas Railroad Commission, a critic of the merger, to transfer some lines and yards to the Texas Mexican Railway Co. "Adding carriers to an already congested and inadequate infrastructure is not going to improve service," says STB Chairwoman Linda J. Morgan.

GULF BEACHHEAD. Davidson's deal, however, carries considerable risk. If the plan—along with other operational changes—fails to assuage angry shippers, UP may face new efforts to amend its \$4 billion merger with Southern Pacific. Federal regulators could, for example, demand divestiture of track and facilities and allow more competitors into the Gulf. Meanwhile, the deal with BNSF—aimed at helping 100 Gulf area chemical makers—could backfire. "BN clearly has its foot in the door in this petrochemical-producing region," notes analyst James M. Higgins of Donaldson, Lufkin & Jenrette Inc. "I think over time you will see far more erosion of UP's business."

If the mood of 300 shippers at a meeting in Houston on Feb. 13 is any indication, that seems likely. As Davidson, a 37-year railroad veteran, explained the new deal to the crowd, he was showered with bitter complaints. "We're up to Plan 650. What's Plan 651?" barked Harry Ignatowski, transportation manager for

to open up temporarily some of its Houston business to competitors. Already attended once, those orders are set to expire on Mar. 15. Shippers expect another extension through August. In Congress, some senators are already promising to review UP's problems when they consider reauthorization of the STB later this year.

Shareholders are also growing impatient with Davidson. Because of the traffic tie-ups, UP lost \$152 million in the fourth quarter, far more than expected. Some analysts predict the company might only break even this quarter. Feb. 18, UP's stock was 60%, down from its high in July of 71%. Davidson and major shareholder Philip F. Schutz, however, denies rumors that



Easing the Gridlock at Union Pacific

UP and rival Burlington Northern Santa Fe propose to:

- ▶ Create a joint dispatching center for all of their Gulf Coast train operations to avoid route and terminal congestion.
- ▶ Exchange half-interests in the two pieces of the 342-mile Houston-New Orleans line now separately owned by each railroad. BNSF wins access to an additional 100 customers on the line.
- ▶ Allow UP to use BNSF tracks between Beaumont and Navasota, Tex., to bypass Houston congestion as needed. UP will not be able to serve BNSF customers on that route.

Dow Chemical Co. Davidson concedes that UP missed its self-imposed deadlines for clearing the traffic jam—and admits that recent efforts, including running trains one way on certain lines and merging the UP and SP computer systems—have created more delays initially. "I don't think there's any silver bullet," Davidson told shippers.

Meanwhile, Davidson has the STB as a semipermanent partner. Last October, the board declared a "transportation emergency" in the West and ordered UP

board has been looking for a new chief executive. "Davidson is doing the right things," says Anschutz.

Meanwhile, shippers have little choice but to wait. "You can't go back," says Robert L. Goodell, an Olin Corp. manager. "The SP doesn't exist any more. And unless Davidson can regain control of his railroad soon, the Union Pacific, in its present form at least, might not either."

By Wendy Zellner in Houston, and Kathleen Morris in Los Angeles

A woman in a dark wetsuit is walking through shallow ocean waves, carrying a large red surfboard under her arm. The sky is blue with scattered white clouds. In the background, a dark, rocky cliff rises from the beach. The overall scene is dynamic and captures a moment of active work or recreation.

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The freedom of Liberty

COMMENTARY

By Peter Coy

THE ANTITRUST COPS SHOULD RIDE THE RAILS

As ungainly oligopolists, such as Union Pacific Corp. and Burlington Northern Santa Fe Corp., take over the nation's railroad service, the Justice Dept. sits and watches the trains go by. It hasn't sued to block a rail merger in nearly 80 years.

Do the feds think everything is hunky-dory on the lines? Not exactly. Justice strongly protested Union Pacific's purchase of Southern Pacific Rail Corp. in 1996. Anne K. Bingaman, then assistant attorney general for antitrust, called it "the most anticompetitive rail merger in history."

No, Justice hasn't sued to block rail mergers for the simple reason that the law prevents it from doing so. That's a mistake that Congress should fix *tout de suite*. When it comes to mergers, there's no reason that a railroad should be treated differently from, say, drug stores or office-supply chains. **DEAF EAR.** Here's the background: Congress gave railroad mergers immunity from Justice scrutiny in 1920 because it worried that overzealous prosecutors were interfering with mergers that would benefit a rail industry then suffering from redundancy and overregulation. Congress gave the Interstate Commerce Commission sole authority to decide on rail mergers. In 1995, when Congress shut down the little-loved ICC, the legacy of 19th century trustbusters, the Clinton Administration wanted to give merger review back to Justice. Instead, after lobbying by Union Pacific, Congress transferred review authority to the ICC's smaller successor agency, the Surface Transportation Board.

The board has been no champion of the consumer. In 1996, its three members approved the huge Union Pacific-Southern Pacific merger, imposing 35 minor conditions. It brushed aside advice from Justice



and shippers that it block the deal or force the combined entity to sell long sections of track to rival railroads. Union Pacific convinced the regulators that the merger would produce—in the words of Drew Lewis, then chairman and CEO—"improvements that truly deserve the term 'unprecedented.'" Since then, the only thing that's been unprecedented is the rapid deterioration of rail service in Texas and beyond (page 42).

To be sure, Southern Pacific was in bad shape when Union Pacific bought it, and the combination may yet improve service for many customers. The Association of American Railroads says railroads have cut average rates in half since 1980, thanks in part to merger efficiencies. But when do railroads get so big that

any increment in efficiency is outweighed by the loss of competition? In light of Union Pacific's travails, it's hard to argue that the Surface Transportation Board always knows best.

NO CHOICE. In the long run, after the traffic jams are cleared, the biggest losers from the UP-SP merger will be shippers who used to play the two systems against each other and are now stuck with a monopolist. In theory, other railroads can serve them by running trains on UP tracks, but customers say that in practice paying costly "trackage rights" makes truly competitive prices impossible. And they're dubious about UP's latest deal to share some track ownership and train dispatching with Burlington Northern.

Monopoly railroads can't get away with overcharging customers who can also ship by truck. But they can sock shippers of coal, grain, ore, chemicals, and other commodities too costly to truck long distances.

"I talk to the railroads and they laugh at me. They say, 'You're not captive, but you're logistically limited,'" says Ward L. Uggerud, vice-president of operations for Otter Tail Power Co. in Fergus Falls, Minn., and chairman of a shipper lobby, the Alliance for Rail Competition.

There's already loose talk about the two big Western railroads merging with the two big Eastern ones to create a pair of transcontinental giants. Do we really want to have the Justice Dept. stuck on the sidings when a deal like that comes down the track? The fledgling Surface Transportation Board comes up for its three-year congressional review this year. Now's the time for Congress to get rail-merger policy right.

Coy is associate economics editor.

Monopolies survive on the tracks. The railroads "laugh at me," says a captive shipper who can't use trucks

EDITED BY KELLEY HOLLAND

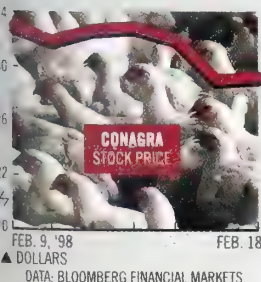
FF-DAVIS DES ON THE BLOCK

FTBANK IS SPINNING OFF its computer trade publication and exposition business. On Feb. 18, the Japanese conglomerate filed to register shares on the New York Stock Exchange in Ziff Davis, which is headquartered in New York and owns periodicals such as *PC Magazine* and *PC Week*, the Internet Web site, and Comdex, the industry's top trade show. The initial public offering, expected to raise \$460 million, could help ftbank to reduce its heavy debt load, brought on by a \$1.5 billion buying spree, and help offset the effects of unfavorable currency change rates. Softbank

LOSING BELL

HERE'S THE BEEF

There's a saying in the meat business: Sell it or smell it. To keep shipments up, ConAgra, the Omaha packer, has been cutting prices—a move that gives investors a whiff of earnings trouble ahead. The problem is oversupply. While U.S. production is up, Asia's woes have damped demand. On Feb. 13, ConAgra announced its earnings would be "far below" expectations for the first half of '98. Its shares have since dropped to 29%. Now, while demand remains slack, U.S. output should taper off.



will also refinance \$1.5 billion in debt.

STORMY WEATHER AHEAD FOR PAN AM

THE NEW PAN AM CORP. IS flying into headwinds. On Feb. 17, the Miami carrier said it was in default on aircraft leases by \$4 million and was negotiating to restructure payments on its fleet. In a Securities & Exchange Commission filing, the airline also said it must come up with \$3.3 million by Feb. 23 to provide additional security for travel-agent refunds. Under David Bamiller, who replaced Martin Shugrue as CEO in November, Pan Am has focused on routes from Florida to the Northeast, laid off 550 workers, and worked to stabilize operations after its merger with Carnival Air Lines.

A FIDELITY MANAGER IS 'NOT SATISFIED'

FIDELITY INVESTMENTS' TOP fund manager is dropping four funds, citing the burden of managing \$43 billion. George Vanderheiden, whose results are second only to Peter Lynch's, says he's turning over control of the Destiny II Fund and three Asset Manager funds to other Fidelity managers. "I'm not satisfied with my performance over the last few years," he says. Indeed, Vanderheiden's funds have trailed the Standard & Poor's 500-stock index for the past two years.

FEDERATED PUSHED DEBTORS TOO HARD

FEDERATED DEPARTMENT Stores has agreed to pay \$14.6 million to settle Justice Dept. charges of improper debt-collection practices. On Feb. 17, Justice announced that a multistate investiga-

HEADLINER: FINN CASPERSON

TIME TO UNLOAD THE FAMILY BUSINESS

It may be the end of a dynasty. On Feb. 17, Beneficial Chairman Finn Caspersen announced that the finance company he had run for 22 years—and his father for 17 years before him—may be put on the block in an effort to enhance shareholder value. The news sent the stock up 37%, to 112%.

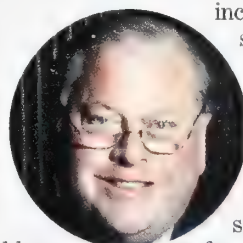
Beneficial wound up in this position because of Caspersen's conservative style. While his restraint kept loan quality high, it kept earnings growth slow. And Beneficial has been slow to upgrade computer systems to bring down the

costs of underwriting loans and collecting payments. Last October, it began a restructuring that was to include the planned sale of businesses.

But analysts such as David Hochstim at Bear Stearns say an outright sale of Beneficial should gain more for shareholders than waiting for the restructuring to bear fruit.

"It is difficult," says Caspersen of a sale. Still, with 278,000 shares, he should benefit nicely from any such deal. That should take some of the edge off breaking a family tradition.

*By Amy Barrett
in Philadelphia*



tion had revealed that Federated was inducing customers who had filed for bankruptcy under Chapter 7 to sign contracts agreeing to repay their department-store debts. Under bankruptcy law, such agreements to repay a debt that otherwise would be discharged in bankruptcy must be voluntary. An earlier investigation led to a similar settlement with Sears Roebuck last year. Federated's department stores include Bloomingdale's, Macy's, and Burdines.

IN AUTO PARTS, THE BIDDING REVS UP

AFTER BEING REBUFFED several times in the past year, SPX, a \$922 million auto-parts maker in Muskegon, Mich., is launching a \$3 billion hostile takeover of Echlin, another auto-parts outfit four times its size—with \$3.6 billion in sales. The news drove Echlin's stock

up by \$11 and spawned speculation on a bidding war in the making. "The reality is that Echlin is now in play," declares Bear Stearns analyst Eric Goldstein. "The only question is who is going to buy it." Write-offs drove both companies into the red last year. Still, SPX is "a terrific turnaround story," says Goldstein. Echlin's board now says that "it will review the SPX proposal in due course." Two factors in Echlin's favor are strict takeover laws in its home state of Connecticut and its own poison-pill protection.

ET CETERA...

- On Feb. 18, a New York Stock Exchange seat sold for a record \$1.8 million.
- Kenny Rogers Roasters is contemplating a Chapter 11 bankruptcy filing.
- Lucent set a 2-for-1 stock split and formed a \$100 million venture-capital fund.

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EDITED BY DOUGLAS HARBRECHT

CHAMBER OF COMMERCE BATTLE CRY: KILL ALL THE LAWYERS

For decades, business and trial lawyers have squared off in courtrooms over everything from dangerous toys to unfair employment practices. Now, the U.S. Chamber of Commerce intends to intensify—and politicize—the battle. In March, it will unleash a multimillion-dollar campaign against longtime foes—and the fight is sure to get ugly.

The chamber is asking its 200,000 members to finance a lobbying and advertising blitz that would target many of the laws and legal procedures that help fill the briefcases—and pockets—of trial attorneys. Among the chamber's goals are new restrictions on product-liability lawsuits, class-action litigation, and contingency fees. It also may push for laws requiring employers who bring discrimination suits or other workplace grievances to pay legal costs they lose. "This would act as a deterrent to frivolous lawsuits," says Lawrence B. Maus, who is running the project.

While business has been seeking tort reform for years, the chamber is ratcheting up the pressure by painting trial lawyers as leeches and vultures who use frivolous suits to line their pockets, raise the cost of consumer goods, discourage manufacturers from bringing products to market, and clog the courts.

It's no coincidence that trial lawyers are among the biggest donors to the Democratic Party, while the chamber's political arm predominantly supports Republican causes. According to the Center for Responsive Politics, the Association of Trial Lawyers of America (ATLA) ranked No. 3—at \$3.5 million—among organizations making political donations in the 1995-96 election cycle.

DICIL REFORM. New chamber chief Thomas J. Donohue promises to turn a spotlight on Washington to make clear who's influencing Congress with how much money. And in states where judges are elected, the chamber will push for laws that would require jurists to recuse themselves if

lawyers before the bench contributed to their campaigns.

The strategy will dovetail with complaints by Capitol Hill Republicans about the huge fees that plaintiffs' attorneys stand to earn if a tobacco settlement passes Congress this year. Those fees could reach \$55 billion if they're calculated at a standard 15% of the total settlement. Both the GOP and the chamber seem to be following a script laid out by pollster Frank I. Luntz. In a report for Republican candidates, Luntz counseled that "it's almost impossible to go too far when it comes to demonizing lawyers." His advice: Describe the "victims of our society's litigiousness" as the small-business owners and homeowners ruined by baseless lawsuits.



DONOHUE: Spotlight on Congress

"JUVENILE." ATLA President Richard D. Hailey contends that the chamber has decided to vilify lawyers to deflect attention from efforts to limit consumers' rights to sue for faulty products or against unfair employment practices. "It's the juvenile approach we object to," he says. "Rather than having an adult discourse on public-policy issues, they are engaging in an anti-consumer, anti-lawyer campaign."

That's a refrain business knows well. Manufacturers have waged a fruitless 12-year effort to pass federal legislation that

would make it harder to sue over defective goods. In recent weeks, business has agreed to give up attempts to cap punitive damages consumers can collect. But the lawyers won't budge on a proposed compromise that would ban suits involving products more than 18 years old. Business strategists intend to use that intransigence to paint the opposition as greedy nitpickers.

The chamber's attack is sure to energize some lawsuit-weary businesses, but it faces obstacles both internal and external. Many chamber members are themselves lawyers already steamed over the campaign. And then there's that citadel of lawyers on the Hill. That's a lot of angry bogeymen.

By Susan B. Garland

CAPITAL WRAPUP

A TAXING EURO PROBLEM

► U.S. multinationals are starting to fret about the tax consequences of Europe's transition to the euro in 1999. One fear is that gains created from converting European bonds or currencies into the new euro will be taxed. Normally, such profits would be taxable only when the holding is sold. But under U.S. law, a company that, say, shifts francs to euros could be hit with a capital-gains liability. Another concern: The conversion could scramble the calcu-

lation of foreign tax credits, which are figured initially in local currencies. Financial institutions, manufacturers, and other companies that will be affected by the conversion have asked the Treasury Dept. to sort out the mess. Sympathetic Treasury officials say they hope to issue guidelines by yearend. The next step may be a hearing before the Senate Finance Committee. Says Carol Dunahoo, a partner in the accounting firm Price Waterhouse: "This is not the sort of thing you want unresolved in 1999."

NEW SPENDING CZAR

► Nine-term Representative C. W. "Bill" Young (R-Fla.) is emerging as the likely candidate to succeed retiring Bob Livingston (R-La.) as chairman of the powerful House Appropriations Committee next year. Young is just as conservative, but he's close to GOP leadership. Livingston is a maverick who has challenged Majority Leader Dick Armey (R-Tex.) on budget strategy. Besides ideology, Livingston and Young share a soft spot for military pork along the Gulf Coast.

SOUTH KOREA

KIM'S WAR ON TWO FRONTS

Both labor and the *chaebol* are ferociously resisting reform

It was a close call. On Feb. 12, Korea's militant labor unions were just hours away from calling a general strike that would have crippled the country's economy. The idea was to force President-elect Kim Dae Jung to drop his plans to make layoffs legal. At the last minute, labor leaders called off the strike, when the lack of public support became evident. Yet even after backing off, the Korean Confederation of Trade Unions made it clear that it would continue to fight any moves to shed workers.

Give credit to the 75-year-old Kim. Since winning the election in December, the former dissident has proven a tough leader willing to stand up to entrenched interests. But with his formal inauguration just days away, the historic struggle to change Korea is just beginning. Although the forces of the old order have suffered some setbacks, they are yielding only stubbornly. Most important, it's not just the unions that oppose Kim's most dramatic proposals. The *chaebol*, the conglomerates that dominate the economy, already are throwing up roadblocks. Unless the *chaebol* change their position, Kim will be fighting a two-front war against labor and

management that could doom serious reform.

Of course, the *chaebol* publicly support restructuring. But privately they criticize Kim's actions. "Kim Dae Jung is pressing for too much too quickly," says a manager at a top company. "He is in such a hurry that he is imposing changes artificially instead of letting market forces to do the job." So the *chaebol* and their supporters have been slowing Kim down, often more successfully than labor. A bill allowing hostile takeovers by foreigners passed in Parliament on Feb. 14—but not before legislators sympathetic to the *chaebol* inserted an amendment postponing implementation

of the law by up to 10 months. Opposition legislators from the Grand National Party have weakened other crucial legislation as well. A new law gives minority shareholders access to company's books. That's a major issue in Korea, where outside investors often have no idea of a company's true finances, or how much profit it is diverting to a corporate parent. The law drafted would have let shareholders look at the books if they held as little as 0.03% of a company's outstanding shares. But at the last minute, the *chaebol* got the minimum shareholding boosted to 1%—a much harder threshold to reach for outsiders. Buying 1% of Samsung Electronics, for example, would cost some \$60 million.

It's not just in Parliament that the *chaebol* and their allies are fighting back. Kim wants the banks to stop lending to big companies at preferential rates. But just in the past six weeks, banks have provided nearly \$1 billion in "emergency relief loans" to sick *chaebol*. Seoulbank provided \$140 million to Dong Ah Group, for example, while Hanil Bank lent \$190 million to Koh Group and \$280 million to Han W Corp. "The loans are offered at far below market rates, and this is a distortion of limited resources



KIM DAE JUNG VS. THE CHAEBOL

CORPORATE GOVERNANCE

Kim wants greater shareholder rights, but the *chaebol* are watering down or delaying laws boosting Kim's position.

BANK REFORM

The new government wants to end preferential bank loans to the *chaebol*. But troubled *chaebol* are still securing below-market loans.

ACCOUNTING

The *chaebol* promise clearer financial reports and an end to secret subsidies of corporate affiliates. But Kim's advisers want concrete proposals.

DATA: BUSINESS WEEK

TOUGH LEADER: But Parliament keeps undercutting Kim

ments Lee Chae Kwang, head of research at Daiwa Securities in Seoul.

One way the *chaebol* get these funds is by asking the courts to help them restructure their loans and procure cheap rates. The banks that lent the money have the right to refuse such court mediation, especially since most of these companies are in such bad shape. But analysts say banks go along with the court requests anyway, just to avoid classifying the loans as nonperforming.

The result is bizarre: Despite a string of widely publicized failures, no big company has shut down any major factory. Hanbo Iron & Steel Co. entered court receivership a year ago, but it is still churning out steel. So is Sammi Steel Co., which failed in March, 1997. Car maker Kia Motors Corp. supposedly collapsed last fall. Yet it keeps shipping cars to the U.S., Europe, and Asia. While other companies are paying interest rates of some 30%, these failed companies are paying half that rate or over as interest," says Min Sang Kee, an economics professor at Seoul National University.

DUMPING? The result is excess industrial capacity that plagues the economy. Four Korean steel companies on Feb. 16 urged Kim's top policymakers to shut off Hanbo's plants to overseas buyers or shutter the company completely, arguing that Hanbo was undercutting prices by up to 16%. Hanbo officials say the company is not dumping, and that Hanbo has just raised its prices.

Some Koreans are getting alarmed that these damaged companies linger on. Rhee Namuh, executive director at Samsung Securities Co., points out that Korean banks risk creating a long-term structural recession by following the example of Japan's banks, which kept offering credit to sick companies so they could not default on loans. "Too much capital is being employed in inefficient industries," says Rhee.

Kim's crisis-management team is aware of the *chaebol's* foot-dragging. His advisers are wondering when companies will produce understandable balance sheets. "The *chaebol* have expressed willingness to improve their financial structure, but their methods are too abstract and their timetables too loose," complains Kim Yong Hwan, head of the team. The big fear now is that Korean companies will soon be able to lay off employees but will still resist calls to restructure dramatically and improve shareholder rights. The result could be rising unemployment, social turmoil—and no fundamental change in the way Korea Inc. runs its affairs. Business as usual. That's the last thing Korea needs.

By Moon Ihlwan in Seoul



TAIWAN

CAN CHINA AIR CLIMB AGAIN?

A tragic crash aborts a comeback in the making

The wreckage told the story not only of the worst airplane crash in Taiwan's history but the second catastrophe in just four years for its leading carrier, China Airlines Ltd. The first time, 264 people died when a CAL A-300 crashed at Nagoya, Japan, in 1994. This time, as rescue workers gathered the bodies of the 203 dead just outside Taipei's main airport on Feb. 16, the manager of CAL's Kaohsiung office knelt weeping before victims' families to apologize—a startling image broadcast on national television. Many who were watching wondered how an airline could be so unlucky, or so poorly run.

Whatever the case, it may be impossible for the airline to complete what had been a painstaking attempt to rebuild its image. Since the Nagoya crash, blamed on pilot error and design flaws, CAL has overhauled everything from in-flight menus to top management. Particular attention was given to improving safety by retraining pilots and hiring Germany's Lufthansa as a safety consultant. Now, with this new disaster and one of the world's worst safety records, CAL is back to square one. "People are not going

to remember the improvements they made, but that they failed again," says Chih S. Fang, ING

Barings Securities airline analyst in Taipei. "People have more choices now."

Those choices include upstart EVA Airways Corp., which has the most to gain. Back in 1994, EVA had only about a 10% share of the market in international flights from Taiwan. It now has 17%, vs. CAL's 29%—a figure that's up from a low of 23% after the Nagoya crash.

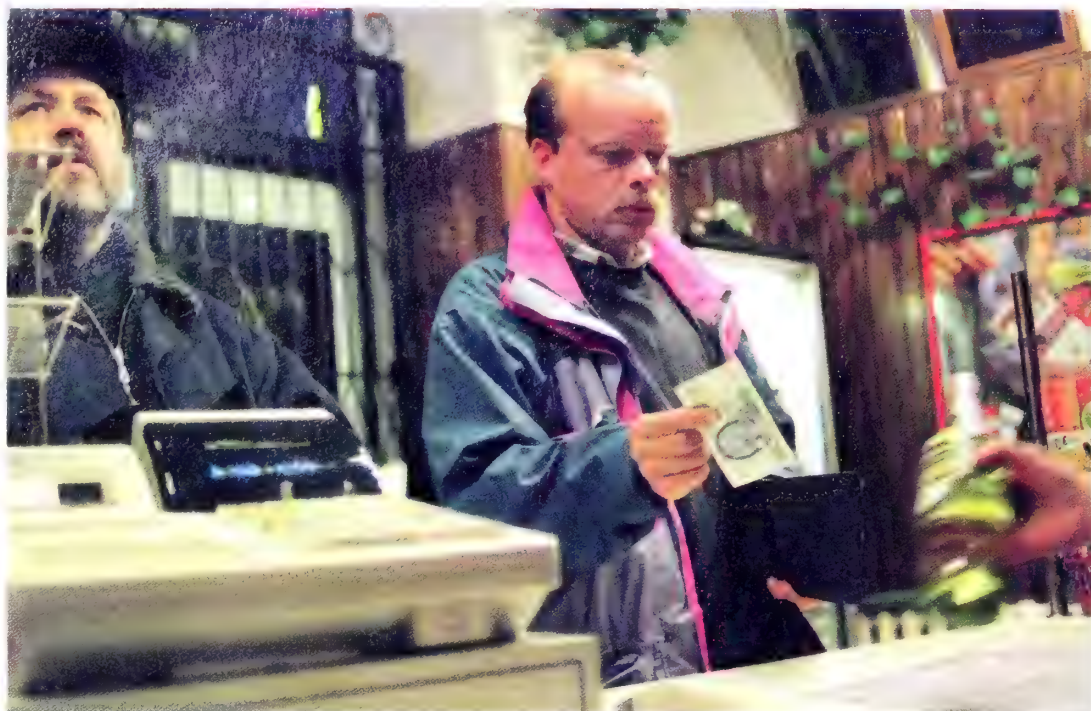
CAL looked to be on the rebound. It was filling a higher percentage of seats even as it added new planes. Earnings were up 60% last year, to an estimated \$90 million, on revenue of \$1.7 billion. Lower fuel and insurance costs, as well as management restructuring, had boosted operating profits. Now, all nine of CAL's A-300s have been grounded pending safety inspection, and CAL Chairman Chiang Hung-I has resigned. Some legislators want to disband CAL.

It's clear that the crash will have a serious effect on CAL for years to come. As Taiwan's former flag carrier in the midst of being privatized, it's still 71% owned by the government-linked China Aviation Development Foundation. CAL likely will have a harder time attracting

a foreign investor to take a 16% stake. It probably will have to curtail expansion plans, and pay out \$40 million in victim compensation. It also faces a vexing question: When you've already done everything you can to improve and it still isn't enough, what else can you do?

By Jonathan Moore in Taipei

ON THE MEND
CAL already had one of the worst safety records in the world, but passengers were returning



VICE PRICE: Hikes in liquor and cigarette taxes will help trim the deficit

POLAND

GET READY FOR ANOTHER 'SHOCK'

Poland's Balcerowicz unleashes another dose of reform

When Leszek Balcerowicz, the fabled father of Poland's economic "shock treatment," reclaimed the Finance Ministry after national elections last September, the burning question was: Can he work his magic again? Many Poles and foreign observers agreed that Central Europe's most vibrant economy desperately needed Balcerowicz and his tiny Freedom Union party to reignite reform, which had slowed during four years of Communist rule. But many also feared he would wield little power in a government led by the Solidarity trade union—with which Balcerowicz enjoys an uneasy political peace.

Now, the 51-year-old Balcerowicz looks set to finish the job he began in 1989. As Deputy Prime Minister and Finance Minister, the former professor wants to keep Poland from degenerating into a once promising also-ran—and secure its place among Europe's first-tier economies. He has already begun a major deregulation drive and has

raised taxes on such things as liquor and cigarettes to get the budget deficit down. He also plans to trim social spending. In the still huge state sector, Balcerowicz is sweeping enterprises clean of political appointees. At the center of his program—call it Shock Treatment II—is a privatization plan

THE BALCEROWICZ PLAN

- Privatize up to 100 of the largest state enterprises, worth some \$40 billion
- Cut regulation in most sectors, but strengthen it in finance
- Reform the out-of-control state pension system
- Rid state enterprises of political appointees
- Trim spending in the overburdened health-care system

DATA BUSINESS WEEK

the previous government had all but forgotten. Privatization is crucial if Balcerowicz is to push for his other reforms—especially plans to tackle Poland's out-of-control pension system.

Problems are inevitable for an age as ambitious as Balcerowicz knows. Some moves could push the 10.5% jobless rate higher. But Balcerowicz is unfazed—although he recognizes that Shock Treatment II will require steady growth

if it is to shake the nation free of the remnants of a planned economy. Poland has been expanding at 7% annually over the last two years. That has made it Europe's star—and encouraged many Poles in their cherished goal of joining the European Union perhaps as early as 2003. Growth should slow to 5% in 1998, but that still gives Balcerowicz plenty of room to push further reform. "It is a crucial mistake to say that reform is going to cause a lot of pain," says the feisty Balcerowicz. "Avoiding reform is what gets very painful."

GREAT EXPECTATIONS. Although foreign investors hung back after last fall's elections, a "Balcerowicz effect" has begun to buoy the markets—and help Poland avoid the Asia jitters hitting other emerging economies. Over the past month the Warsaw stock market is up 25%, to 16,600. A sale of \$2 million worth of treasury bills on Feb. 9 was nearly four times oversubscribed. The surge of foreign capital also helped hold the zloty firm—even forcing the central bank to intervene to keep the currency from appreciating. Says Barbara Lundberg, executive vice-president at Enterprise Investors, a Warsaw-based venture capital firm: "There are huge expectations with Balcerowicz coming back."

Investors are looking closely at Balcerowicz' much-hyped privatization policy, which is aimed at the 35% of Polish output state companies still accountable for. In March, Balcerowicz will unveil

ans to sell up to 100 large state enterprises, worth some \$40 billion. Those les could begin later this year.

The new minister has already hasened—and enlarged—several large privatizations. In the biggest, 20% of one company Telekomunikacja Polska, worth \$3 billion, will be sold via a ock offering this year. The remainder will go to foreign strategic investors by 2000. By contrast, the previous government had planned to sell st 15% this year and to prohibit foreign ownership. In addition, half of retail banking group Pekao will go on e block this year, up from an earlier anned 15%. And Polish Airlines-LOT ecently signed an agreement with ritish Airways PLC that is probably a elude to a partial sale. The previous overnment had blocked foreign investors in this deal, as well.

ENSION PIT. At Balcerowicz' insistence, the new coalition has also been eaning up executive suites. Nine one company directors who were political appointees have been replaced o far this year. Jan Monkiewicz, who ismanaged insurance giant Powszechny Zakład Ubezpieczeń so badly that e company's loss reserves slipped 257 million below legal requirements, ft the company and was replaced by adysław Jamroz, a respected industry veteran. Warsaw is also holding own wages of government workers, hich are budgeted to rise only 1.5% is year, vs. 4.5% last year.

The toughest part of Balcerowicz' econd act will be social security. The ate pension system sucks up 17% of ll spending; millions of Poles collect ensions and work in the underground onomy. While plans to partially privatize the system have been agreed pon, the reform will require a budget-busting \$2 billion annually for the ext decade. Meanwhile, the cash-trapped health system is also unaveling. It is wracked by strikes and, lthough care is officially free of charge, patients must often bribe doctors to get the medical attention they want.

Amid such challenges, there's still a anger that the political peace Balcerowicz helped forge will fall apart. The Solidarity Election Action party, s the coalition is called, is cobbled toether out of about 40 different factions, from religious radicals to socialists. What unites them is a deep conviction that the former Communists an never again be entrusted with Poland's future. And so, with a gulp, hey're all resigned to another bout of hock treatment.

By David Woodruff and Peggy Simpson in Warsaw

COMMENTARY

By Julia Flynn and Stanley Reed

ASTRA: TIME TO TAKE A STAND, MR. BARNEVIK

Since taking the chairman's seat at Investor 10 months ago, Percy Barnevik has launched a high-profile effort to modernize the Wallenberg corporate empire. He has installed new executives and pushed for cost-cutting at companies the Wallenberg holding company owns major stakes in. And he has called for diversifying the clubby boards of Wallenberg companies—part of his plan to boost shareholder returns.

Now, Barnevik faces a sterner test than he bargained for in Astra, the Wallenbergs'

largest holding, representing 27% of their portfolio. Astra's stock has underperformed over the past year, reflecting worries about its prospects. CEO Håkan Mogren is under fire for failing to develop hot new drugs and for losing control of top lieutenants, some of whom have been accused of

sexual improprieties and misuse of corporate funds. Now, with litigation pending, Mogren is being accused by former executives of fostering a corporate culture that encouraged such abuses through his own high living at Astra's expense. Mogren denies the accusation.

If Barnevik is serious about reform, he must deal decisively with the strategic and sleaze problems at Astra. He should launch his own investigation of what has gone on at the company and oversee a strategic review. Mogren may have to step down. After raising hopes that the Wallenberg empire will become more accountable to shareholders, it's time for Barnevik to deliver. Otherwise, he risks letting Astra slide into the margins of the global drug industry. Says Lars-Erik Forsgardh, CEO of the Swedish Shareholders Assn.: "Everybody expects [Barnevik] to do something about the situation at Astra."

Barnevik won't comment. Investor says Astra must sort out its own

problems. That's ducking responsibility. Investor is Astra's biggest shareholder, controlling 12% of its voting stock. Astra's chairman is Bo Berggren, a longtime Wallenberg exec; its vice-chairman is family scion Marcus Wallenberg; and Investor President Claes Dahlbäck also sits on the board. They may be reluctant to discipline a close associate: Mogren serves on the Investor board and those of Wallenberg companies Stora and Incentive.

Investor executives seem to be in a quandary about what to do at Astra.

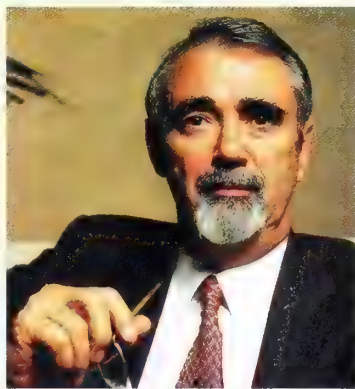
They have taken the line that nothing beyond personal excess is wrong with Astra—insisting that Mogren is the victim of a witch hunt, brought on in part by his haughty style. They also note that Astra's stock has been the hot performer in their portfolio until recently. "Discussions" are going on between the board and Astra's management, an In-

vestor executive says, but major changes are unlikely soon.

Astra's problems go far beyond high living. Its former U.S. head, Lars Bildman, has pled guilty to filing false tax returns in the U.S., and two other honchos have left under clouded circumstances. The Swedish prosecutor's office is about to depose one of them, Astra's ex-Nordic head, Anders Lonner. That could lead to new disclosures about Astra's corporate practices and Mogren's spending habits.

Like it or not, Barnevik may have to face a stark choice: Fix Astra quickly or allow the drugmaker to derail his plans to forge the Investor companies into a top-flight global network. Astra has delivered stellar returns for the Wallenbergs and other shareholders over the years. But that's no excuse for ignoring problems that could get even uglier and more painful if they are allowed to fester.

BUSINESS WEEK's Flynn and Reed cover Swedish business.



BARNEVIK: Astra needs his help

COMMENTARY

By Ian Katz

HOW LATINS CAN SURVIVE THE ASIAN STORM

Since Asia's crisis erupted last year, Latin Americans have complained that their markets are being unfairly tarred by events beyond their control. The region's healthier economies and better-managed banks, Latins argue, should not be linked by skittish investors to Asia's woes. Like it or not, though, investors see both regions as part of the same emerging-market class. "The worst of the Asia crisis is behind us, but we're still not the masters of our destiny," says former Brazilian central bank chief Francisco R. Gros.

That's why major Latin stock markets are down an average 10.5% this year, despite strong fundamentals in Brazil, Mexico, and Argentina. Initial public offerings, which gained momentum in 1997, have been put on hold. And the yield gap between Latin debt and U.S. Treasuries remains wide: around 300 basis points for Brazil's five-year notes, compared with 140 before the crisis hit.

UNEASY. To hold back the Asian shock, Brazil has raised interest rates, cut spending, and pledged to defend its currency. But investors are still uneasy, with reason. The region's deficits in trade and current accounts could worsen, putting new pressure on currencies as Asian competition in world markets revs up. For Brazil and Argentina, the ratio of foreign debt to exports—a key measure of their ability to pay their way—is about 300%, or three times what most analysts prefer. So despite extensive free-market reforms in recent years, Latin America still has a lot to do before it can be considered a safe haven—or at least a breed apart from riskier emerging markets.

In the short term, some govern-

ments will have to keep economic growth in check to curb import demand. For Brazil, that means holding growth to 2% or less this year. But a top priority must be to beef up exports. President Fernando Henrique Cardoso hopes to double Brazil's annual exports to \$100 billion by 2003, aided by export promotions and in-



First, cut imports and beef up exports; then slash bureaucracy and endemic corruption

centives. But to expand exports long-term, Latin Americans will have to boost productivity by spurring industrial efficiency

and improving infrastructures.

The U.S. must do its part, too. "Moving forward with free trade would be reassuring to the markets," says Richard Feinberg, former adviser to President Clinton on Latin American affairs. "It would show that the U.S. is behind Latin Ameri-

ca." For starters, the U.S. Congress needs to find common ground between Democrats and Republicans to provide authority for Clinton to launch hemispheric trade talks.

To attract foreign investors, Latins also must create a more business-friendly environment. Throughout the region, maddening bureaucracies and complicated regulations and tax systems impose heavy burdens. In February, Ford Motor Co. said it was considering cutting back on future investments in Argentina because of high production and labor costs. The latter are raised by rigid labor-market restrictions and union health-care monopolies that President Carlos Menem has been slow to overhaul.

To escape from the emerging-market stigma, Latin America will have to pursue even deeper reforms, such as curbing endemic corruption. At a BUSINESS WEEK conference on Latin America in February, 57% of participants, many of them multinational executives, said they had been asked for bribes. And while privatizations have become a linchpin in Latin America's conversion to free markets, they must become more transparent and better organized. In recent weeks, investors have been scared away from Brazil's cellular B-band sales by long-running legal wrangles over the bidding process.

Latin America's surges of reform in the early 1990s, and again following Mexico's 1994 peso collapse, were a good beginning—but not enough, as it turns out, to assuage jittery investors' fears of contagion from Asia. What's encouraging is that the latest threat has helped mobilize broad support in key countries for even more fundamental reforms. This time, leaders should seize the chance to make sure the region will indeed be a safe haven the next time an emerging-market crisis erupts.

Katz covers Latin America from São Paulo.



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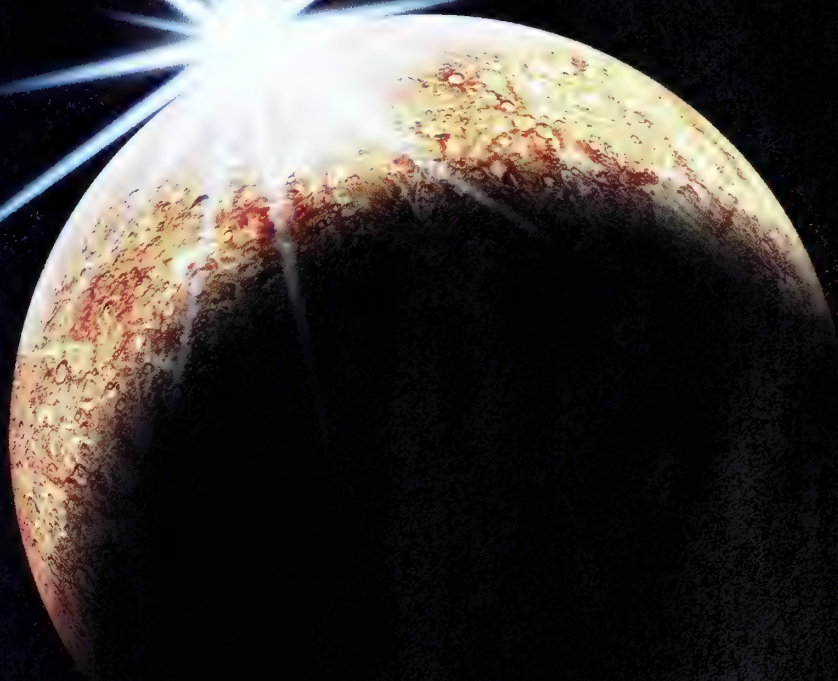
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CHINA: ZHU IS TAKING BROOM TO THE BUREAUCRATS

China's economic czar, Zhu Rongji, summoned the country's 60 top bureaucrats to a crucial meeting last fall. He asked the ministry bosses to justify their jobs as the country shifts from a planned to a market-driven economy. "If you don't have a job to do, you talk and I won't," he warned. "Next time, talk and you won't." Now, Zhu is ready—and many of the mandarins won't like what they're about to hear.

The hard-driving Zhu is expected to announce the biggest cleanup in decades of China's state ministries. At the National People's Congress, due to start in early March, Zhu will replace the wooden Li Peng as Prime Minister. He is expected to shutter or merge some 10 ministries. Some will be converted into holding companies, while many companies once run by ministries will be spun off into separate, self-governing entities.

Zhu is facing tremendous resistance; on a roster of 10 million officials, 2 million jobs are in jeopardy. Debate on details of the reforms still rages behind closed doors at Zhongnanhai, the leadership's headquarters, as intricate power games are played out. The Electronics Ministry, for instance, swings between becoming the core of a new superministry for information technology and disappearing altogether. Many government officials blame Zhu personally for the upheaval.

ON ITS OWN TERMS. As the Congress nears, though, it's clear Zhu is prevailing. While the redundant mandarins may cling on to their perks, such as housing and health benefits, they have largely lost their battle against early retirement or transfer. Beijing's leaders recognize that the central government badly needs a massive overhaul.

So far, China has managed to escape most of the financial devastation that has shaken other Asian nations. But there are ominous signs that Beijing is not immune. Growth this year could fall below 8%, the level that sets alarm bells jangling in Beijing.

Foreign investment, too, is expected to drop for the first time in 20 years, with export growth slowing to just 5% from 22% last year.

With Asia's economic meltdown rattling the Beijing leadership, Zhu and his supporters now have a powerful argument that China must get its own house in order to prevent meddling by the International Monetary Fund or other outsiders. "China wants reforms carried out on its own terms," says a Western diplomat in Beijing.

Paring down China's top-heavy government is key to speeding reform of state enterprises. Zhu plans to hive off companies that were under the thumb of ministries. He also wants to reduce the conflicts of interest facing ministries that are both regulators and competitors. The Post & Telecommunications Ministry, for example, regulates the industry and also controls China Telecom and regional phone companies. Analysts say it may lose all its operating businesses to become just a regulator.

Zhu is looking for other efficiencies as well. Some analysts say the Ministries of Labor and Personnel will be merged. The same fate may await the Culture Ministry and the Radio, Film & Television Ministry. Meanwhile, the Internal Trade Ministry will likely become part of either the Foreign Economic Trade & Cooperation Ministry or the State Economic & Trade Commission.

But Zhu's transformation of China will require at least one new ministry—for social security. Already, as many as 12.5 million workers are unemployed as state enterprises go belly-up, estimates researcher Hu Angang. By 2000, an additional 10 million jobs will disappear.

Zhu must avoid a social explosion as he steers an unwilling bureaucracy toward mending its ways. If he can implement his reforms fully, Zhu will indeed have the last word.

By Joyce Barnathan and Dexter Roberts in Beijing



MOVE OVER: Zhu and Li Peng

GLOBAL WRAPUP

U.S. BLOCKS AGREEMENT

The Multilateral Agreement on Investment among rich industrial countries is unlikely to be signed on schedule in April. U.S. negotiators insist that business, environmental, and labor groups must be consulted first. The agreement aims to set a level playing field for international investment. But the U.S. objects that the agreement would stop state and local governments from regulating foreign investors.

At a Feb. 16-17 meeting in Paris,

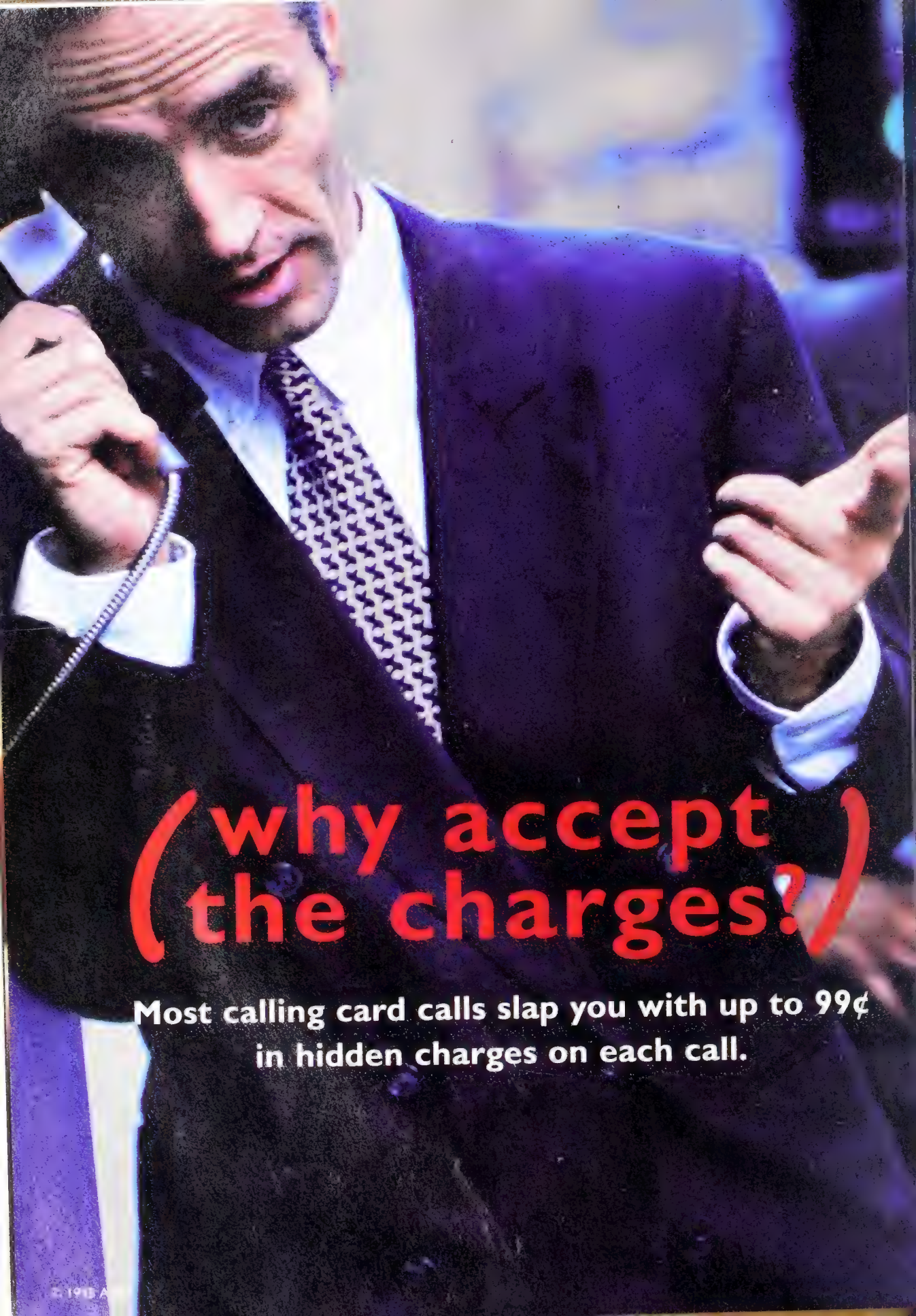
the U.S. delegation, which was led by Under Secretary of State Stuart Eizenstat, received assurances that the 147-page draft agreement would soon be made public. The U.S. is also unhappy about European Union attempts to favor EU investors over outsiders.

INDONESIA ANNOYS IMF

► The International Monetary Fund is fast losing patience with Indonesia. It is threatening to suspend further installments of a \$43 bailout package after Indonesian President

Suharto sacked central bank governor Soedradjat Djiwandono on Feb. 17. The governor, a respected proponent of prudent banking, free exchange rates, and IMF-backed reforms, objected to Suharto's plans to set up a currency board.

Suharto regularly thumbs his nose at the IMF. Cronies, with his apparent approval, are showing blatant disregard for at least two other IMF conditions: abolition of the Apkindo plywood and Bulog flour monopolies. But the sacking of Soedradjat was the last straw.

A man in a dark suit, white shirt, and patterned tie is talking on a corded telephone. He has a stressed or frustrated expression, with his forehead wrinkled and his mouth slightly open. His right hand is holding the phone receiver, and his left hand is raised in a gesturing motion. The background is blurred, suggesting an office or public space.

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DETROIT'S IMPOSSIBLE DREAM?

Fuel-cell cars on the road by 2004—that's the promise. Now it's crunch time

Two years ago, Bradford B. Bates of Ford Motor Co. predicted he wouldn't live to see cars powered by the space-age devices that are his passion—fuel cells—because that would be three decades in the future. Now Bates, who's 60 and a key fuel-cell researcher at Ford, says he expects to be able to purchase an electric car powered by the devices "before I give up driving." Indeed, he's now striving to fulfill Ford's promise to put a fuel-cell car on the road by 2004. Quips Bates: "I never apologize for being smarter today than I was yesterday."

Propelled by political and competitive pressures, Detroit has made an amazing conversion to environmentalism. Until now, the auto industry has been an environmental bad guy, lobbying fiercely against any treaty that would limit auto emissions in an effort to mitigate global warming. Now, barely a week goes by without one of the Big Three announcing an initiative to tackle global warming or reduce dependence on fossil fuels.

Most startling of all, though, is the pledge to bring out fuel-cell cars by the middle of the next decade. Suddenly the fuel cell, once found only on NASA spacecraft, has become Detroit's pet project for "going green."

Fuel-cell cars would appear to be the perfect antidote to today's ozone-depleting, smog-making vehicles. Through a chemical reaction between hydrogen and oxygen, fuel cells generate the juice to power an electric motor—and the only emission out the tailpipe is a trickle of water. The technology is even ahead of current electric cars, with their limited-range batteries and long recharging times. With fuel cells, drivers would "recharge" by filling up at the same ser-

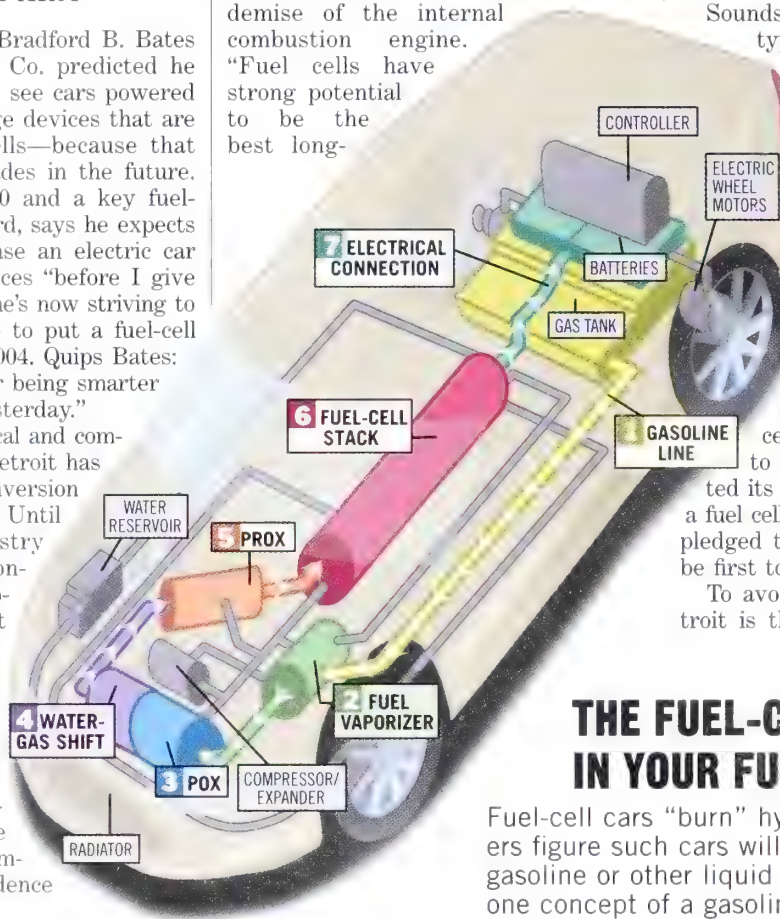
vice station they've always used. That's because new technology can extract hydrogen gas from liquid fuels.

As a result, even Detroiters are predicting what was once unthinkable: the demise of the internal combustion engine. "Fuel cells have strong potential to be the best long-

term solution," says General Motors Vice-Chairman Harry J. Pearce. "Our fuel-cell test vehicle gets 80 miles per gallon and has a driving range of 300 miles."

Sounds wonderful. But GM's prototype, like all the others in Detroit, hasn't left the lab yet. Mercedes-Benz and Toyota Motor Corp. have actually rolled out operational fuel-cell vehicles—but they're not yet for sale. Mercedes showed a tiny A-class car in September with a backseat and trunk stuffed with the various high-tech gizmos. Toyota's company is aggressively pursuing the technology and predicts it will sell 40,000 fuel-cell cars annually by 2006. Not to be outdone, Toyota has unveiled its RAV4 sport-utility vehicle with a fuel cell, and President Hiroshi Okuda pledged this month that Toyota would be first to market such a car.

To avoid being left in the dust, Detroit is throwing hundreds of millions



THE FUEL-CELL CAR IN YOUR FUTURE

Fuel-cell cars "burn" hydrogen, but auto makers figure such cars will sell only if they run on gasoline or other liquid fuel. Here's a look at one concept of a gasoline-powered fuel-cell car.

- 1 GASOLINE LINE** Feeds liquid fuel from the tank to the fuel vaporizer.
- 2 FUEL VAPORIZER** Heats gasoline to convert the liquid to gases.
- 3 POX** The partial oxidation reactor combines gasoline vapors with air, producing hydrogen and carbon monoxide.
- 4 WATER-GAS SHIFT** Steam acts as a catalyst to convert most of the carbon monoxide to carbon dioxide and additional hydrogen.
- 5 PROX** The preferential oxidation unit injects air to convert the remaining carbon monoxide into carbon dioxide, leaving hydrogen-rich gases.
- 6 FUEL-CELL STACK** Hydrogen gas is chemically combined with oxygen, producing electricity for the motors that propel the car.
- 7 ELECTRICAL CONNECTION** Coordinates the electric motors that make the wheels spin. Also, a nickel-metal-hydride battery propels the car initially until the fuel-processor system warms up.

DATA: ARTHUR D. LITTLE, CHRYSLER CO.

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at fuel-cell technology. Ford is investing \$420 million to join with Mercedes and fuel-cell supplier Ballard Power Systems Inc. in Vancouver, B.C. Chrysler Corp. has hooked up with GM's Delphi unit, an auto-parts supplier, and expects to be cranking out 200,000 fuel-cell cars by 2010. And GM is reassigning legions of engineers to fuel-cell development and boosting their budget, according to company officials. "As the heat turns up, the dollars come in," says Andrew J. Farah, GM's engineering manager of battery systems.

SAFETY QUALMS. Yet despite the influx of cash and talent, the auto makers face daunting technical challenges to meet their new deadlines. "Our target to commercialize these vehicles by 2004 has a lot of risk," admits John R. Wallace, Ford's director of alternative-fuel vehicle programs. Bates puts it bluntly: "We don't know how to get there."

Cost is the biggest roadblock. If a Ford Taurus were outfitted with a fuel cell today, its sticker price could soar to \$200,000, says Ford Chairman Alexander J. Trotman. That's because an electric car needs about 80 kilowatts of power for acceptable performance. With fuel cells, the per-kilowatt cost now stands at roughly \$250. So just the fuel cell would run \$20,000. Add on the tab for several other expensive elements (illustration, page 66), and a fuel-cell car is 10 times more costly. The per-kilowatt cost hasn't changed for two years. So why the new optimism? Detroit now expects it can slash costs to \$25 per kilowatt, from the previous target of \$35, says Bates. For now, though, that's just a dream. "It's amazing how the hurdles get higher," says Ballard Power Chief Financial Officer Mossadiq S. Umedaly.

Still, there has been substantial progress. Ten years ago, a fuel-cell vehicle would have cost \$20 million—and only a city bus could have accommodated those hulking devices. Engineers have since shrunk the size needed for a car to something on the order of a suitcase. And the costly materials used in fuel cells are being replaced or the quantity needed is being reduced. For example, the cost of platinum used as a catalyst on the electrodes of an 80-kw fuel cell has dropped from \$33,000 in 1984 to \$500 or less. Projecting these trends forward, Umedaly says that by 2008, when Ballard expects to be producing 250,000 fuel cells annually, they'll cost no more than a traditional engine.

As fuel-cell costs have come down, however, another obstacle has risen: the need for an onboard fuel "refinery" to

extract hydrogen from a liquid fuel. Selling consumers on the safety of modern techniques for storing hydrogen gas could take longer than perfecting an economical fuel-cell car. "Most of us remember the Hindenburg," says GM's Pearce. Besides, nobody wants to mount a torpedo-like storage tank on a car's roof. Finally, there are no hydrogen filling stations now—and building the infrastructure for distributing hydrogen to corner service stations would take billions of dollars.

That's why auto makers plan to run fuel cells on methanol or gasoline, using

The environment takes a hit with ADL approach, though. Extracting hydrogen from methanol or gasoline produces carbon dioxide as a by-product, although only a fraction of the CO₂ that combustion produces. "The fuel cell has great potential, but it's certainly not the solution to global warming," says David E. Cole, director of the University of Michigan's Office for the Study of Automotive Transportation.

Another problem: It takes 10 minutes to warm up a fuel processor. Until then, the car must run on a 500-pound nickel-metal-hydride battery, which r



Ten years ago, a fuel-cell car would have cost \$20 million. Now, it's \$200,000 and dropping

GM SHOWS OFF ITS TECHNOLOGY AT THE CHICAGO AUTO SHOW

a so-called fuel processor to tap the hydrogen contained in the liquid. But these minirefineries are in their infancy—"at the stage that fuel cells were 5 or 10 years ago," says Christopher E. Barroni-Bird, Chrysler's head fuel-cell researcher.

Pulling hydrogen from gasoline was first demonstrated last October. The processor was developed by Arthur D. Little Inc. (ADL) of Cambridge, Mass., in conjunction with the Energy Dept. ADL plans to announce on Feb. 24 the formation of a company, Epyx Corp., to sell the processor, which can also suck hydrogen from methanol and ethanol, a corn-based fuel. "There used to be tremendous scorn for our technology," says Jeffrey M. Bentley, vice-president and technology director at ADL. "Now we get board-level attention."

costs \$20,000. "That's completely unacceptable," says Barroni-Bird. "We need it to be less than one minute" to shrink the heft and cost of the battery.

PROMISES, PROMISES. Other pieces of the fuel-cell puzzle are falling into place. Impressive progress has been made developing transmissions, for instance. While consumers haven't flocked to battery-powered cars, the R&D that went into them helped Detroit cut the cost and improve the reliability of the motors and generators. Insiders say that GM, thanks to its EV1 electric car, has an edge in electronic controllers, which coordinate all the high-voltage operations of the drive system. By 2000, the sources expect GM to have an electric transmission equal in cost to a traditional automatic transmission.

Still, researchers may have trouble keeping up with the public-relations machine. Already, engineers are looking for wiggle room in the pronouncements by senior managers. Even Ford's Barroni-Bird has a hard time accepting the newfound optimism. "We really have no confidence these things will completely deliver on their promise," he admits. "But the promise is so great, you just have to give it a go." Or risk seeing more German and Japanese cars in driveways.

By Keith Naughton in Detroit

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A MEETING OF MINDS IN PHILADELPHIA

Science takes on diodes, disease, dopamine, and the defense of Dolly

150th gathering of the American Association for the Advancement of Science had a distinguished guest list: President Bill Clinton opened the event in Philadelphia last week with a call for strong antitobacco legislation. Also in attendance were Ian Wilmut, who cloned the famed sheep Dolly; U.S. Surgeon General Dr. David Satcher; and U.S. Supreme Court Justice Stephen G. Breyer, who discussed science in the courts. Here are some of the highlights:

LASER DIODES MAKE QUANTUM LEAP

ERICO CAPASSO, A SOLID-state physicist at Bell Laboratories, says he has created a new type of laser on a chip—a laser diode—that is as practical and 100 times more powerful as existing diodes. Today's laser diodes, commonly used in bar-code readers and CD-ROM drives, give off photons of light when electrons and positively charged "holes" recombine on the chip. Capasso's diode works on a different mechanism—quantum-mechanics effect known as resonant tunneling, in which units of charge cascade down a series of quantum "waterfalls," giving off photons with each jump. For the new diodes, that means a single electron can release some 25 photons, instead of just one, says Capasso. And there's another advantage: The color, or wavelength, of light can be tuned for different purposes by altering the thickness of the chip's layers. Conventional laser diodes, in contrast, require different materials for each color. Capasso and his team first demonstrated their cascade devices in 1994. But those devices worked only when cooled to very low temperatures. The new device performs at room temperature, which makes it commercially viable. "There's nothing comparable out there," Capasso says. He pre-

dicts that the lasers will first be used as long-range sensors—to measure air pollutants from as far as two kilometers away. *John Carey*

HEALTHY GENES FOR UNHEALTHY LUNGS

GENE THERAPY HAS BEEN long on promise but short on results. The basic problem is delivering the genes. For example, to treat cystic fibrosis, scientists have inserted correct copies of the gene that causes the illness,

using a virus as the delivery "vehicle." But in clinical trials, the new gene never worked for long. And repeated treatments tended to make things worse, provoking immune responses against the virus.

Scientists at Genzyme Corp. say that in recent tests they got better results using molecules called lipids as a delivery vehicle. When the molecules, which get gobbled up by target cells, were hitched to correct versions of the CF gene and inserted into patients' lungs, the benefits lasted up to several weeks. The results provide hope that an improved lipid, already being developed at Genzyme, could provide an effective treatment, says Genzyme senior director Seng H. Cheng. *John Carey*

IS DOLLY A REAL CLONE OR A FLUKE?



WILMUT: Other scientists cannot replicate his results

Wilmut was forced on the defensive by comments from Norton D. Zinder of New York's Rockefeller University and Vittorio Sgaramella of Italy's University of Calabria. Noting that Dolly was the only success out of 400 cloning attempts, the scientists described the experiment as "an anecdote, not a result." They complained that no other researcher has been able to repeat the results and suggested that Dolly may have been made from an easier-to-clone fetal cell—not an adult cell, as reports claimed. Wilmut denounced the criticism as "premature," saying: "There simply has not been time" for others to replicate the results. *Paul Raeburn*



WHY CHOCOHOLISM WILL NEVER DIE

THE LATIN NAME FOR THE cacao tree, *Theobroma*, means "food of the gods," and who wouldn't agree? Now, researchers have discovered that no other food can satisfy the craving for chocolate, even if the substitute contains many of the same chemicals.

A recent University of Pennsylvania survey found that one-third of adults say they regularly crave chocolate—which could be why yearly U.S. consumption is 12 pounds per person. Scientists had assumed that the craving was linked to one or more of the 300 chemicals contained in chocolate, such as substances similar to caffeine and dopamine.

Not so, says Paul Rozin, a Penn psychologist. He asked 30 volunteers to record the effect of various substances on their yen for chocolate. Coffee didn't dull it, nor did capsules of cocoa powder. Other combinations of cocoa, sugars, and fats fared only slightly better. The only food that reduced the craving was an actual chocolate bar. "There's just something about having this wonderful substance in your mouth," says Rozin. Warning: Testing this theory could cause weight gain. *Catherine Arnst*

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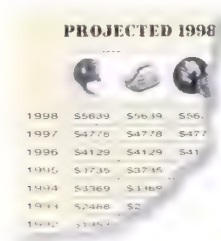
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In Box page 2

Stuff and Sense

Small-business incubators, successful family firms, Clinton's small biz rep, and more



Finance page 4

The Off-Balance Sheet

A day in the life of nonbank lender Allied Capital shows it weighing assets like vision and personal integrity

Companies page 8

What Asian Crisis?

When the Thai economy tanked, Derk Wilken leveraged a battered baht by selling cheaper Web design in borderless cyberspace



Marketing page 12

Ahead of the Curve

Trend-spotting isn't just for companies marketing cutting-edge products, and amateurs can actually be better at it than pros



Technology page 18

Sharebrained

From quirky niche products to alternative office applications, shareware has unique advantages

Roundtable page 22

Why the Lady is a Champ

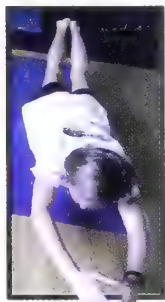
Once Renee Fellman shows up at a troubled company, the prospects quickly improve. The turnaround artist discusses her benign interventions



Government page 24

Where's the Beef Board?

The SBA's Regulatory Fairness Program investigates complaints about enforcement actions or specific agency regulators



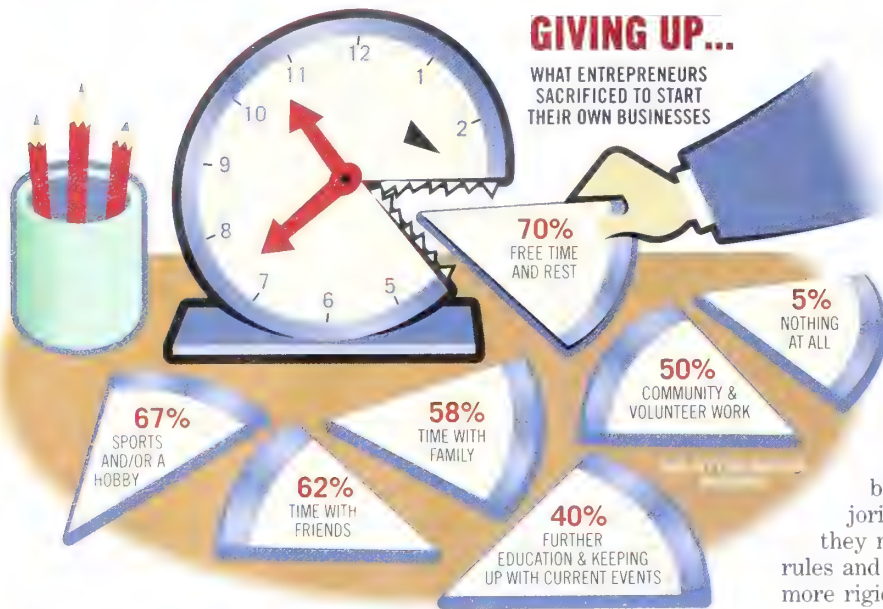
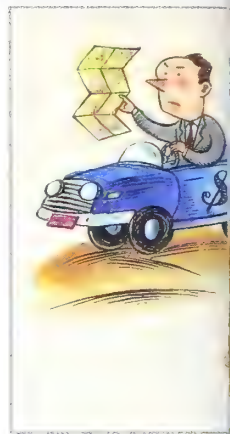
Downtime page 26

The New Schmoozing

Gen-Xers and women are getting down with clients in ways that don't involve three courses—or golf courses

IN BOX

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...AND GIVING BACK

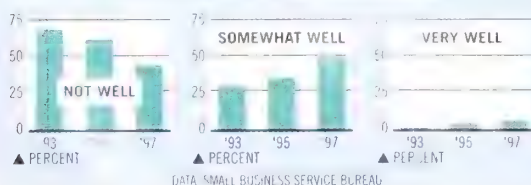
Perhaps their own sacrifices make small-business owners more responsive to employees' personal needs. In a survey last fall by Wirth Worldwide, 58% of 400 business owners with sales of \$1 million to \$3 million said balancing work and family is a major part of their workplace culture. Just 28% of Fortune 1000 executives gave a similar response in a Wirthlin poll two years ago. Although they have fewer resources and less flexibility than their corporate brethren, a majority of small-business owners told Wirthlin they manage to offer employees flexible work rules and schedules. A solid minority, however, is more rigid.

HOW'S HE DOING? NOT BAD



Even small business is warming to Clinton. In 1997, 2,600 business owners gave him better approval ratings than he has had so far, in a rolling survey conducted by the Small Business Service Bureau. Just four years ago, Clinton had the worst numbers in the poll's 15-year history. Only 6.4% think the President is helping "very well," but his '97 score is the best since 1986, when Reagan had 11% strongly approving and 31% disapproving. Why? The economy, stupid. The poll also showed fewer respondents paying interest rates above prime or suffering tax increases.

"HOW WELL DO YOU THINK THE PRESIDENT IS HELPING SMALL BUSINESS?"



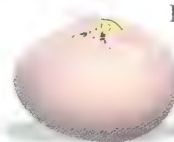
ALREADY

82% have business casual dressing	11%
47% allow job sharing	26%
49% use temps, part-timers, or consultants	31%
53% have compressed workweeks and flextime options	25%
26% let workers telecommute	46%

WOULD NEVER

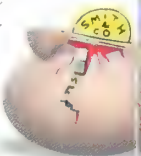
SOURCE: KEY CORP. WIRTHLIN WORLDWIDE

EARLY CODDLING CAN ENSURE Y



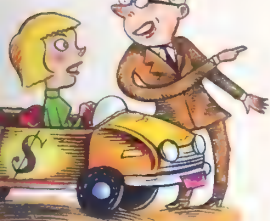
Entrepreneurs know it's easier to hatch an idea than a company. Now, a Commerce Dept. study suggests that the odds of success improve for companies born in business incubators, which typically offer space plus support services.

A random sampling of startups in incubators between 1990 and 1996 showed their sales expanded fourfold on average between the time they entered and the time they left (usually two to three years). Annual sales grew an average of \$239,535. What's more, of the startups that "graduated" from incubators between 1980 and 1991 (less than 10% drop out), 87% are still in business.



SMALL COMPANIES HIRE PROPORTIONALLY FEWER BLACKS BUT MORE HISPANICS

I'M NOT LOST



The car isn't the only place men are reluctant to ask for directions. A MassMutual/NFWBO poll shows more women business owners take advantage of outside sources of information than their male counterparts.

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DATA: MASSACHUSETTS MUTUAL LIFE INSURANCE COMPANY NATIONAL FOUNDATION FOR WOMEN BUSINESS OWNERS

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HOW TO AVOID A DYSFUNCTIONAL FAMILY BUSINESS

Family businesses are famously susceptible to bitter, divisive battles; 88% fail by the third generation. Searching for the keys to long-term success, James Hunt, a management professor at Babson College (huntj@babson.edu), studied five successful family firms that are at least 20 years old, ranging in size from two to 200 employees. Several characteristics the firms shared amount to "best practices" for family-run companies. 1) *A focus on business, not family, needs*: Don't use the business as a family employment agency or loan center. 2) *Reinvestment*: Don't suck the company dry. 3) *Caution with family*: Forestall potential conflict with precautions, such as two or three months of debate before hiring family or dispensing generous severance packages to discourage draining litigation. 4) *Delegation*: Don't be a control freak. 5) *A big-picture view*: Consider all stakeholders—from employees to local community—in making decisions.



Among others, Hunt studied Nancy Jones and her brother Cameron Kelley, who share leadership duties as principals of Cameron Inc., a Boston-based graphic design firm their father founded 40 years ago.

SO THEY SAY

"People just don't bring somebody else in to run their company unless they have serious problems. It's like giving your child up for adoption."

—Renee Fellman, a turnaround specialist, who rescues troubled small companies (page 22)

MANAGING

MERGERS

GLING COMPANY FLIES

In comparison, the Small Business Administration estimates 62% of all new companies close within six years. There are now more than 600 U.S. business incubators, up from 12 in 1980. Sponsored by nonprofits, universities, or private groups, each has its own acceptance criteria. Many incubators provide management advice, office services, and financial, legal, or tech help, too. Service companies lead the list of clients, at 35%, ahead of light manufacturing (23%) and technology firms (22%).



For more about incubators, visit BWPlus! at www.businessweek.com or America Online at keyword BWEnterprise.

WHAT LARGE COMPANIES DO, ACCORDING TO U.S. GOVERNMENT DATA

To buy or not to buy? That's the question many small companies face in this era of consolidation. For fast-growth outfits, at least, acquisition is a hot strategy, notes a recent Coopers & Lybrand survey, which asked 425 small-company CEOs to rate how their own deals turned out. Recent acquisitions were called "extremely or very successful" by 65% and "somewhat successful" by 22%. But about 10% of CEOs admitted their deals had not gone so well, citing incompatible top managements and ego on one or both sides as key trouble spots. Asked what they would advise others to look out for, they warned against: succumbing to time pressures (63%), not doing enough homework (62%), impatience in negotiation (56%), and misreading one's own corporate strengths and weaknesses (56%).

INSIDE THE MIND OF A SMALL-BIZ LENDER

Allied Capital finds that it often pays to look further than the balance sheet

Louis M. Coco '88, the managing director of a small New England manufacturing, was just days away in May, 1996, from clinching a \$5 million loan to finance a buyout of the company from its owners when a potentially devastating new problem cropped up.

"I've been having tests done on my heart," Coco remembers telling Philip A. McNeill, an investment banker at Allied Capital Corp., describing the heart attack that struck while he was at the New York City Opera. "It turns out I've got some major blockage," he recalls saying matter-of-factly, "and they're recommending I go in for bypass."

As a principal at Allied, a Washington D.C.-based lender to small and mid-sized companies, McNeill had confronted all kinds of obstacles to getting deals approved. But a quadruple bypass on a CEO was a first. Now, it was his turn to feel ill. After months of analysis, background checks and basic hand-holding, the end had been in sight.

Still, McNeill caught something in Coco's long-distance demeanor. Less than a day after hearing such devastating news, the entrepreneur was calm, focused, and sharp—managing this personal setback the way he probably would run his business. Besides, the fi-

going to support you," he remembers telling Coco.

NO MISSES. Good call. Almost two years later, Coco is still at the company, Julius Koch USA Inc., a New Bedford, Mass., maker of parts for window blinds. The company hasn't missed a single payment on its 13.5%, eight-year loan.

Not all borrowers are so fortunate. Each year, about 37% of small-business owners shop for a loan and bankers reject a quarter of them, outright, according to a 1996 study by Arthur Andersen accounting.

But with competition heating up amid small-business lenders, there's less reason to take "no" from a bank as a final answer. While banks still do the bulk of small-business lending at about \$172 billion a year, they're under pressure from Allied, the Money Store, GE Capital, and a host of other nonbanks, which dole out another \$96 billion a year to small companies—sometimes in spite of what their regular bankers think.

So who gets the money? What makes a lender agree to finance a company that someone else rejected? The answer—which hinges on the strength of a business, its vision, and the owner's personal integrity—becomes quickly apparent if you spend a day at Allied headquarters.

Allied is among the top 10 nonbanks dealing in loans backed by the Small Business Administration. Overall, the publicly traded company has amassed 500 investments worth about \$600 million. Some of that includes simple real estate mortgages, and another large chunk includes commercial mezzanine loans like the one Coco received. The latter are subordinated debt, a risky deal for Allied, so the lender makes up for it by charging up to 15% interest, plus warrants to acquire equity.

Better deals are available from Allied's SBA-backed loans, which offer up to \$1 million at only 10%. Why so much less? Because the SBA repays 75% of the principal if a company defaults. It's an attractive niche for Allied, which last year lent \$52.6 million to 82 companies after sorting through 1,000 applications.

Mondays at Allied start with the regular weekly partners meeting held in the company's ninth-floor conference room. Eight top officials are huddled around an oval table, including Chairman William L. Walker, 48, and seven top officials.

The 10 deals arrayed in front of the are already survivors of a sort. Sometimes deals come over the transom; others are referred by accountant lawyers, and financiers who know Allied's appetite. But all have passed through the initial round of digging Allied's staff into the borrowers' financial and personal backgrounds. Companies stand a better chance if the most rece-



KOCH'S COCO: A loan despite his surgery

The "Non" Factor

When it comes to small-business credit, banks still dominate, but nonbank lenders have made big inroads.

CREDIT TYPE	MARKET SHARE		
	BANK	NONBANK	OTHER*
COMMERCIAL LOAN	64%	30%	6%
LEASING	33	60	7
VEHICLE	61	39	0
EQUIPMENT	65	32	2
COMMERCIAL MORTGAGE	77	20	3
LINE OF CREDIT	93	7	0

*Based on 1996 revenue. *Includes family, friend, government



al year included growing sales, posi-
e cash flow, and a net profit, though
marounds are also considered.

The meeting itself is a relaxed give-
-take, with Walton presiding in shirt-
eves and red suspenders. The for-
t: One person pitches his or her
orite deal. Everyone else tries to
e holes. Winners move on to the
t step, the investment committee,
eventually, the 22-member board of
ectors.

DOUBLE DIP. It's a rapid-fire affair, with
h deal getting less than 15 minutes
fame. The first concerns a pair of
men entrepreneurs seeking an SBA-
ked loan to buy a grocery store in
al Michigan; they're on the verge of
duating to the investment committee.
e borrowers couldn't be happier, and
SBA loves this deal," reports princi-
Mary E. Olson. (Olson says the
ncy favors disadvantaged companies,
d this one qualifies twice: it's rural,
d the owners are women.)

Walton worries more about the com-
petition. "How far is the nearest super-
market?" he demands.

"About 10 miles," Olson says. "In the
idle of winter, 10 miles is a lot."

"How long has the business been
und?" Walton asks.

"About 45 years," she says.

entrepreneur can often achieve more than what the numbers suggest"

"That's a long time," Walton says ap-
provingly. The idea gets the nod. Other
deals get quick approval, too: expansion
of a successful Popeye's Chicken & Bis-
cuits franchise in Virginia, in part be-
cause of its plentiful free cash flow; a
broadcaster's plan to deliver foreign-
language TV programming via satellite
to the growing U.S. immigrant popula-
tion from Eastern Europe.

A home-improvement products com-
pany meets more resistance. It's emerg-
ing from a recent bankruptcy.

"How did he handle his creditors?"
Walton asks.

"Nobody lost any money," Olson says.

"His suppliers are happy?" Walton
presses.

"He's got credit terms from all of
them," Olson counters. The team agrees
to table this one until they check the
receivables.

What is Walton looking for? Sure, a
company has to clear certain financial
hurdles, including \$1.40 earnings for
every dollar in fixed costs, debt of no
more than four times equity, and re-

turn on net assets of 20%. Intangibles
such as the power of a brand name
count, too. But in every case, there's a
single bottom line: "You have to start
with great management," says Walton.

After a break, Walton convenes the
investment committee, a decidedly less
forgiving group. While the earlier meet-
ing was open and creative, this panel is
judge and jury. "We need to have all the
answers at that point," Walton says.

He isn't getting them today. The deal
concerns a promising chemical company
that wants to expand. But the amount
of unsold inventory seems swollen com-
pared with overall sales—perhaps busi-
ness is slowing—and the thought nags
at Walton as the meeting goes on. "I'm
not ready," he finally declares, sending
the deal back for more due diligence.

Such probing begins at the first con-
tact and doesn't let up until the loan
check is cashed. Sometimes, the ques-
tions can get intensely personal. Just

CEO WALTON:

"We've discovered
that a good

ask Henry E. Juskiewicz, CEO of
Nashville-based Gibson Guitar, who got
a \$25 million, 15% interest loan package
last summer. "Allied called virtually
everybody I know... dozens of people,
and asked very pointed questions about
me as well as management," he says.

Good or bad, the answers aren't the
kind of data you can get from trendy
tactics like credit scoring, a method used
by nearly all banks that grades appli-
cants based on statistical norms for
small business. Walton says the system
can mislead lenders, because the norms
are based on business conditions of the
past and tend to miss promising aspects
of the future. "Over the years," Walton
says, "we've discovered that a good en-
trepreneur can often achieve more than
what the numbers suggest." Apparently,
vision and passion are still assets you
can take to the—well, nonbank.

By Jonathan Burton in Washington

For information on finance leads online, visit
BWPlus! at www.businessweek.com or on
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HOW TO FIND THE LENDER WHO WAS MEANT FOR YOU

Ready to go hunting for your own private lender? Good luck. If you spent a dollar mailing your business plan to each potential prospect, you'd need a \$15,000 loan just to contact them all.

The trick is to zero in on the most likely partners. Most lenders specialize in a particular region or industry that they know well—manufacturing, retailing, or technology, for instance. And while some relish the idea of lending to an untested startup, others won't touch a company unless it's been around for several years.

DON'T DESPAIR. One way to improve your odds is with a go-between, such as a lawyer, accountant, or investment banker who knows the lending market and the appetite of each player. If you don't find a match on the first try, don't despair; a financier who trusts the go-between may well refer you to a lender who is more likely to take on your kind of company. The hope, says Nolan Lehmann, president of Equus Capital Management Corp. in Houston, is that the other lender will reciprocate. "Even if it's someone who calls over the phone, we might try to refer them," Lehmann says.

If you can't get plugged in to that network, try one of the Web's loan finders. These free, interactive searches are the financial equivalent of computer dating. You fill in the blanks and the service creates a list of potential lenders. Two of the more promising sites are America's Business Funding Directory (www.businessfinance.com), which claims more than 15,000 sources, and MoneyHunter's Golden Rolodex (www.moneyhunter.com), which boasts more than 4,000. By giving specific information on your industry, type of financing, size of the loan, and size of your company, you'll quickly pare the list to a manageable size. For instance, we asked Business Funding Directory what was available for a five-year-old publishing

company with \$5 million in sales and fewer than 50 employees that was seeking \$1 million in asset-backed loans. The search turned up more than 100 potential matches, complete with contact names and telephone numbers. The list included giants such as GE Capital Small Business Finance in St. Louis, commercial

Business Funding Directory, but a few thousand is suspicious. Ask for references, and be wary of funds that supposedly come from overseas. Verifying that the money even exists before you pay the upfront fees may be impossible.

You might also try browsing the online roster of federally licensed

Big Names in Small-Business Loans

The 10 largest nonbank lenders of SBA-backed loans in fiscal 1997, ranked by dollar volume.

LENDER	NO. OF LOANS	VALUE MILLIONS	PHONE NUMBER/ WEB SITE
THE MONEY STORE	1,763	\$784.0	800-998-6888 www.themoneystore.com
AT&T SMALL BUSINESS LENDING	1,254	480.5	800-713-4984 www.attcapital.com
HELLER FINANCIAL	916	401.3	800-347-6430 www.hellerfin.com
GE CAPITAL SMALL BUSINESS FINANCING	248	149.4	800-447-2025 www.ge.com/capital/smallbiz
INDEPENDENCE FUNDING	192	108.5	800-225-1776 www.independencelifunding.com
BUSINESS LOAN CENTER	158	105.0	800-722-5626 (no Website)
EMERGENT BUSINESS CAPITAL	123	96.6	888-354-3277 www.bothears.com
COMMERCIAL CAPITAL	323	89.5	888-749-8707 www.commercialcapitalcorp.com
ALLIED CAPITAL	82	52.6	888-818-5298 www.alliedcapital.com
BUSINESS LENDERS INC.	145	42.6	800-646-7689 www.businesslenders.com

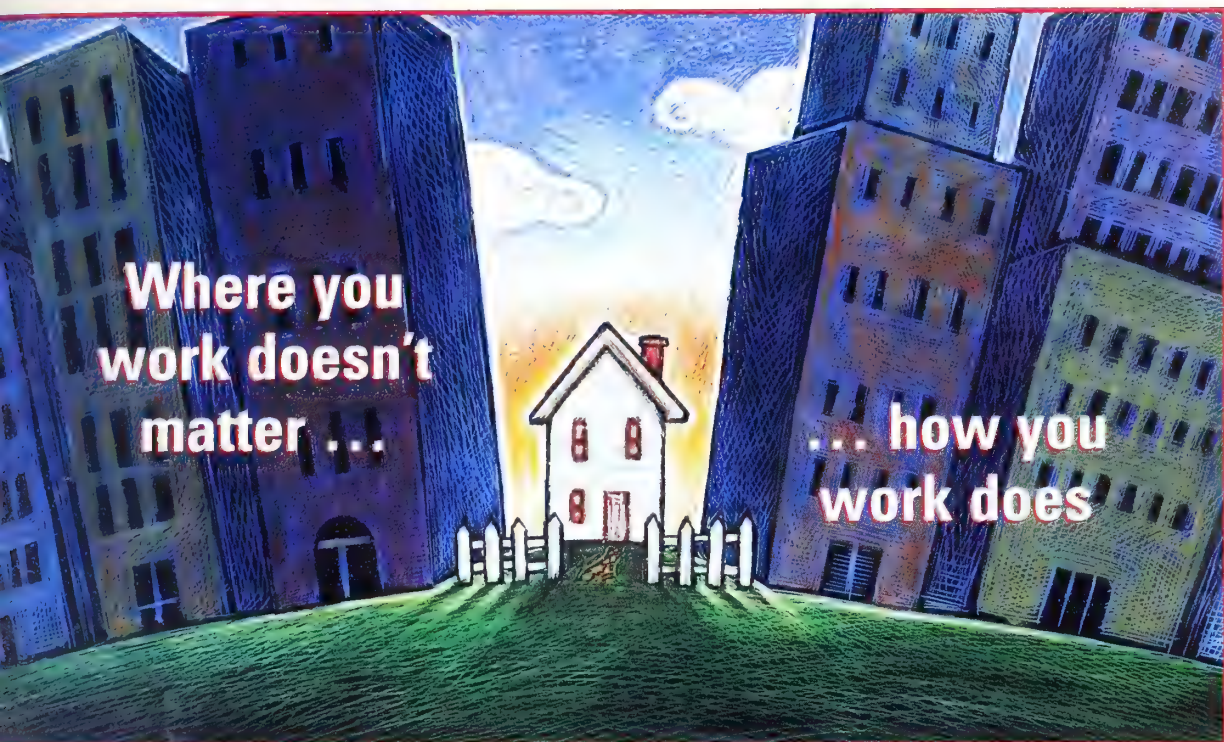
DATA: COLEMAN REPORT SMALL BUSINESS ADMINISTRATION

credit specialists such as Finova Capital Corp. of Phoenix, Ariz., several big commercial banks, and a host of smaller lenders from around the country.

The services say that they make an effort to screen out unscrupulous companies, but some slip through. Red flags include huge up-front fees. A few hundred dollars might be reasonable, says a spokeswoman at the

Small Business Investment Companies (www.sbaonline.sba.gov/cgi-bin/print_hit_bold.pl/sbainfo/fainy/sbical.txt). There's no search function, but the list is a gold mine of names, contacts, and the type of loans each prefers to make—well worth the effort of scrolling through. After all, a treasure hunt isn't supposed to be too easy.

By Rick Green in New York



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*Rates apply to domestic long-distance calls only and are subject to change. Certain restrictions apply. Connection fees apply for international and Operator-assisted calls. Toll-free and FONCARD calling card calls from a payphone will be assessed an additional surcharge to cover FCC-mandated payments from long-distance carriers to payphone providers.

BWEEB 3/98

MAKING THE MOST OF A MELTDOWN

How Derk Wilken is steering his Web-design firm, Beebop, through the Asian crisis

When Derk Wilken started his Web design firm, Beebop Internet Services in Bangkok 10 years ago, he expected to ride the economic wave of Thailand's booming economy. But a year later many businesses were closing—including Beebop's first client, a travel agency, which shut down in January 1997 without paying its bill.

Wilken rejected the suggestion of his Thai friends that he hire off-duty police officers to collect. Instead, he swallowed the loss and kept the defunct agency's Web site online to advertise his work, and realizing that he couldn't afford to leave his home country. Wilken launched his own E-mail marketing business in 1997, and business in the berspace and took "beyond the horizon of Thailand, because on the Web, the whole world is your market."

Wilken's moves **BANGKOK —AND BEYOND** have paid off. The company has 10 employees and a turnover of \$1 million a year. "The whole world is your market,"

Wilken says. "When others stand idle, and the baht fetches only about half as many U.S. dollars as it did last July, when

BEACH LOVER. Even so, tugging Beebop's turnover down to \$220,000 last year, about \$22,000. And if

the baht falls further, Wilken's income will drop. He's diversified his income by becoming a cigar importer and a real estate agent.

In recent months, new

Philip Morris Asia, London magazine publisher and Asia's largest newspaper publisher, have all turned to Beebop for Web design and



the baht falls further, Wilken's income will drop. He's diversified his income by becoming a cigar importer and a real estate agent.

Thailand, Wilken claims he can set up a complex Web site for one-third of

As businesses around the world confront rising wages for scarce technical workers on their home turf, they can outsource parts of their computer programming and Web design work global-

ly. "Long-distance working relationships are becoming the norm," says Ober. Philip Morris Asia Inc.'s chief executive, Michael Ober, hired Beebop last July to build and maintain a Web site for the company in Hong Kong. He has also worked to Beebop, too.

Low-cost business, Wilken's career

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ENTERPRISE

Companies

has bridged East and West. A Dutch national, he spent four years as a procurement officer with the U.N. in New York, Singapore, Thailand, and the former Soviet bloc. But his fondness for beaches and a job in procurement for international aid agencies led him back to Thailand in 1995. Within a year, he quit to pursue a longtime interest in the Internet.

Wilken taught himself Web design and in January, 1996, launched Beebop out of his apartment. He liked the name's "swing"—and it was an easy English word for Thai speakers to pronounce. For startup capital, he pooled his own savings with a \$10,000 loan from his brother in Germany. And to comply with laws that limited foreign ownership, Wilken found a partner: Jirabool Vitayasing, owner of Dash Creative Co., a trinket manufacturer. The two companies swapped 30% of their shares. In September, 1996, Beebop moved into Dash's offices in suburban Bangkok. Today, Beebop still shares Dash's secretary, bookkeeper, and sometimes its graphic designers.

While Dash has been invaluable locally, Wilken's newsletter—which now has about 500 subscribers—has been his key to building business around the world. It's easy and cheap to produce and has, directly or indirectly, hooked important clients. AutoAsia's publishing director, Steve Fisher, was surfing the Web one day for cheaper Web-design work when he could find in London. After stumbling onto Beebop's Web site (www.beebop.com), Fisher followed directions for subscribing to the newsletter. Impressed by Wilken's marketing expertise, he hired Beebop to build a fee-based Web database. "I wanted someone who understands marketing, and it didn't matter to me where they were," says Fisher.

While it's common for small busi-

nesses in Thailand to impress clients with fancy addresses, sleek offices, a posh car, Wilken has always been frugal. He doesn't have a car—takes taxis to visit clients. His office spare. Besides Wilken, Beebop has a part-time Web developer. His first timer starts next month. Salary: around 15,000 baht monthly—or \$330. Wilken supplements with student freelance

He concedes his frills approach cost him some local business but thinks he's better prepared to handle adversity than most Web firms there.

Web designers had hoped to do business locally, particularly vulnerable. "We expect more corporations to use the Internet, but it's not put up Web sites each year, but with the economic crisis they have postponed plans," says Prai Ratanachathong, executive director of Idea Net Co., a small Internet service provider in Bangkok. Wilken, too, has a new local business wither but has persuaded his existing Bangkok clients stay on board by stressing the Web value as a low-cost marketing tool.

To continue

offshore expansion, Wilken is mostly getting small and midsize businesses trumpeting his ability to set up intranets and Web sites with big databases might not be able to afford otherwise. He plans to ramp up his marketing efforts with trips to Europe and the U.S. this summer. Last July, he incorporated in Las Vegas—chosen because of its regulation—and set up a U.S. bank account—just in case some clients push that he have a U.S. presence. Eventually, says Wilken, "we may absorb other companies," in Bangkok. But he's in a rush: He takes his lesson from a volatile economy. A slow, steady pace—with a lot of time for some lazy beach days—may be the right speed.

By Aparna Mukherjee in Bangkok
with Robin Schatz in New York

SURVIVAL STRATEGIES

To pull through Thailand's crisis—and possibly profit from it—Beebop Internet Solutions is:

- ▶ Exploiting the devalued currency by offering low-cost services to non-Thai companies, particularly smaller businesses that can't afford to build their own Web-site databases and intranets
- ▶ Highlighting its ability to help clients sell to the Asian market
- ▶ Promoting services through Beebop's Web marketing newsletter, distributed by E-mail throughout the world
- ▶ Sharing office personnel and real estate space with a partner
- ▶ Taking advantage of falling wages to build staff and using student freelancers to keep costs even lower
- ▶ Persuading financially strapped local businesses to keep their Web sites as a low-cost marketing tool

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TREND-SPOTTING: ANYONE CAN PLAY

And sussing out the latest craze may point you toward a profitable future

Hobart C. Buppert III, known as "Hoby" to his friends, was club-hopping in Vienna four years ago when he was introduced to a popular nonalcoholic beverage that cost \$10 a can. Dancers were swilling the sludgy brew like it was "some sort of powerful elixir," recalls Buppert. The drink was actually loaded with caffeine—from guarana beans.

When the young Cornell University hotel school grad got back to the States, he noticed other trends: the proliferation of coffee bars; the tendency for clubgoers to alternate booze and soft drinks to sustain all-night dancing; and the growing rage for natural ingredients and gimmicky foods such as no-fat ice cream. Also, Buppert noticed people complaining about fatigue and stress. Eventually, he connected the dots, and launched Hoborama Corp., based in Miami. His first product was "Bawls Guarana," a soda with three

times the caffeine of Coca-Cola Classic. The soda popped—catching on in dance clubs in south Florida, southern California, and New York. Now, it's in grocery stores in those states and spreading to Europe too.

Buppert, now 24, developed his business idea not by using reams of pricey research, but simply through observation. That same kind of trend-spotting is done by well-hyped research companies such as Youth Intelligence, BrainReserve, and Iconoculture. Major corporations, including Sony, McDonald's, and Sprint, pay big bucks for their insights.

But you don't need to hire a consultant. "Anyone can be a trendmeister," says Larry Samuel, a partner in Iconoculture and co-author of *The Future Ain't What It Used To Be*. In fact, says Faith Popcorn, chairman of BrainReserve and probably the best known of her breed, you might even outsmart the

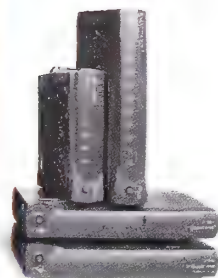
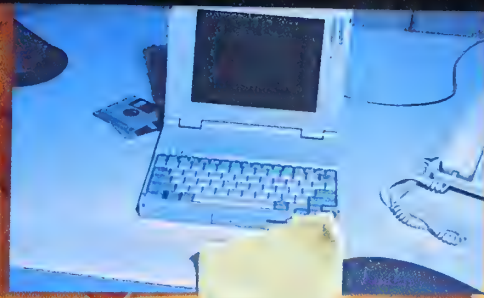
pros. "Amateurs are actually better at it," she insists. They aren't "restrained by the rigid structures of education, all of the false wisdom." In other words, they can often see the obvious more easily than the experts.

Trend-spotting isn't just for entrepreneurs looking to start new companies or for marketing cutting-edge products. Consider, for example, the growing cultural emphasis on well-being. Take that trend, says Mary Meehan of Iconoculture, and you'll see several trends—the yearning for mental and physical health; a desire for greater pleasure in one's life; a revitalized interest in hearth and home; and a new focus on spirituality.

The response: Grocery stores are stocking natural and organic foods, medicinal herbs, and nontoxic cleaning supplies. Some insurance companies have expanded to cover alternative medicine. Hardware stores are carrying a

TRENDS

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Marketing

water purifiers, nontoxic paints, and test kits for detecting contaminants such as lead.

How do you start? Remember, valuable information is everywhere you look. Try to see things the way the marketing gurus at big companies do. For example, Linda Lewi, senior vice-president for global brand marketing at Rockport Co., a division of Reebok International Ltd., reads about 30 magazines a month to spot recurring themes. When she noticed an optimistic tone in a skateboarding 'zine, she saw it as a sign that young people were becoming more upbeat. She had Rockport incorporate a cheerier tone into its advertising. The result, she says, was increased sales.

On the surface, it doesn't seem that a gasket manufacturer should care that avocado or magenta are hot fashion colors. But it's wise to file away such pieces of information for future reference. As Karen D. Seratti, senior mar-

BRAIN TRUST: You can create your own by testing your theories on smart acquaintances of various ages and incomes

keting research analyst for American Century Investments, based in Kansas City, Mo., suggests, using popular colors in marketing materials could make customers pay closer attention. "It's the color people are responding to," she says.

Also, examine whether the fads around you add up to the deeper, wider trends that can suggest business opportunities. "It's like being an outfielder," says Samuel. "You don't move to where the ball is, you move to where the ball is going."

That's just where former stockbroker Tim DeMello hopes he has landed with Streamline Inc., his computerized concierge service that lets customers order such items as groceries, rental videos, wine, and even pet supplies on the Internet. He fills the orders from his own warehouse every Friday.

DeMello, 38, is an information junkie who spends 10 hours a week scanning magazines, newspapers, and the Web and watching TV news shows. He noticed five years ago that home delivery businesses had proliferated far beyond pizza and that polls showed Americans felt time-starved and hated supermarket shopping. And he determined that Web commerce had come of age, judging by the success of the Internet book-seller Amazon.com, and the ubiquity of Web business addresses.

Streamline, based in the Boston suburb of Westwood, Mass., already has attracted 3,500 local members at \$30 a month, and the company recently raised \$10 million in financial backing from investors,

including Intel, GE Capital, PaineWebber.

As DeMello has learned, diligent search can pay off, and it's a lot cheaper to do it yourself. The pros often charge \$25,000 for an initial consultation and another \$75,000 for specific advice tailored to your company. Instead, do the next-best thing and buy their books, which are frequently updated (table) or scan Web sites, forums, and e-mail rooms. And read as much as you can. Create your own brain trust by testing your theories on smart acquaintances of various ages and incomes. Some hunches can, of course, still be confirmed with cold, hard numbers, the kind of research offered by Research Starch Worldwide Inc. and pioneer Yankelovich Partners Inc., which have been publishing its trend predictor, *Monitor*, since the late 1960s. And the U.S. Census Bureau keeps an accessible database with all sorts of demographic information. Or you can hire an outside survey company, such as Motivation Inc. in Schaumburg, Ill. (table).

ALIENS ARE OUT. But nothing really substitutes for trend-tracking in the field. Look, talk, and listen at home, clubs, parks, stores, or wherever you gather. Besides, stalking the next big trend can be fun—especially if you have to shop, like Jane Rinzler Buckingham, the president of Youth Intelligence, a professional trend-spotting firm. Visiting she takes to the wilds of the Westchester Mall in White Plains, N.Y., wanders her way through a number of specialty stores, carefully noting what's selling well—massage products, lotions, scented candles, simple clothes—what's not: anything with almond-scented aliens on it.

Her conclusion? Stressed-out consumers are trying to reward themselves with small indulgences. She cautions, though, that her prey is elusive. "You expect a trend to jump out at you," she warns. "It emerges over time." And even if you do miss a trend, never fear. There'll always be another one coming right behind it.

By Roy Furchgott in Baltimore

TREND-SPOTTING

THE FUTURE AIN'T WHAT IT USED TO BE: THE 40 CULTURAL TRENDS TRANSFORMING YOUR JOB, YOUR LIFE, YOUR WORLD

Vickie Abrahamson, Mary Meehan, Larry Samuel, Riverhead Books \$27.50

The partners of Iconoculture forecast trends such as "bunkering." (Home as sanctuary from the hostile world.) Subtrends—and often an accompanying business opportunity—are discussed, too.

CLICKING: 17 TRENDS THAT DRIVE YOUR BUSINESS—AND YOUR LIFE

Faith Popcorn and Lys Marigold, HarperBusiness \$14

BrainReserve cites 16 current trends, from "cocooning" to "vigilante consumers" and explains how to become your own futurist.

ROCKING THE AGES: THE YANKELOVICH REPORT ON GENERATIONAL MARKETING

J. Walker Smith and Ann S. Clurman, HarperBusiness \$25

Smith and Clurman examine attitudes and values of Matures, Boomers, and Xers and suggests how to forecast and capitalize on their patterns.

THE U.S. CENSUS BUREAU: <http://www.census.gov>

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BEFORE YOU BUY THAT SOFTWARE . . .

Check out shareware—it's cheap and it (usually) works

Dick Nethercot was in paperwork purgatory. The Wichita entrepreneur had built Bill Griffing Painting Inc., the 40-year-old house-painting firm he had purchased three years earlier, into a local powerhouse; more than a dozen men worked for him, and his annual revenues stood at nearly \$1 million. But success meant his increasingly elaborate billing needs could no longer be handled manually. So, in the spring of 1997, Nethercot began hunting for software. After installing Intuit Inc.'s QuickBooks Pro, the leading small-business accounting program, he decided it was too complex and laden with features he didn't need. Instead, he chose a simple billing program, Financial Freedom Billing Manager Pro, from tiny M&R Technologies Inc. of Palm Bay, Fla. "It turned out to be a slick little program that did everything we wanted it to do," says Nethercot. Not only that, he was able to download the program from the Internet and test it out before sending M&R a dime.

As Nethercot learned, sometimes the best answer to business software needs isn't on retail shelves. Instead, it may be found in the class of software known as shareware, which is typically sold directly by the software developers over the Internet or distributed on CD-ROM. Some shareware, dubbed "freeware," is gratis, but other programs can cost anywhere from a few dollars for a simple utility, such as a powerful onscreen calculator, to about \$80 for a sophisticated image editor. Some easygoing programmers work on the honor system, while others build in automatic expirations after a certain period if you fail to pay for registration.

The shareware concept harks back to 1982, when two software developers, lamenting the paucity of affordable programs for IBM's fledgling personal computer, offered their own handiwork to friends and associates, asking for a \$25 donation to cover costs. Customers were encouraged to copy the programs and pass them on, provided they kept the program—and the payment request—intact. Checks started pouring in, and a new industry was born.

SOFTWARE

Today, you can choose from thousands of shareware applications, from esoteric programmers' tools to full-featured word processors, spreadsheets, and database managers. Some admittedly seem like the primitive fruits of a college student's all-night programming binge, others match leading commercial products on features and ease of use. Shareware users, by industry estimates, spend some \$100 million a year on registration fees—a drop in the bucket compared to mainstream software purchases. But industry experts also estimate many users go uncoun-tered because they never pay for the software.

Low price was shareware's first big attraction, particularly to small businesses on shoestring budgets. But that advantage has largely evaporated as mainstream software grows cheaper and more programs come preinstalled on PCs.

So why consider shareware at all? For one thing, there's the try-before-you-buy option—so popular some big software companies mimic. Then, too, many shareware fans cite its personal touch and minimalist appeal. "Shareware offers business a chance to deal directly with the author of a program, instead of a middleman," says Nethercot.



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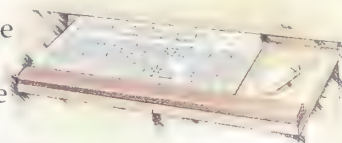


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BIG MENU: Shareware ranges from quirky niche products to alternatives to the top office applications

some big corporate entity," says Richard Holler, the executive director of the Association of Shareware Professionals (ASP). This can be especially helpful because many shareware programs are industry-specific: There are programs for real estate agents, dentists, hotel managers, and accountants, among others. For a small business unlikely to have the tech staff to write custom programs or the clout for discounts on mainstream software, this in-depth industry knowledge, coupled with accessibility, can make a real difference.

Take the experience of shareware loyalist Stuart Levy, a Staten Island (N.Y.) accountant. For almost eight years he has used Medlin Accounting, shareware written by Jerry Medlin of Napa, Calif. The two are on a first-name basis. "I've had a good rapport with Jerry," Levy says. "He's made many improvements to the product over the years, some at my behest." When Levy suggested that Medlin add a way to easily input recurring entries, the feature appeared a few weeks later. "I've dealt with major software companies," says Levy. "They're courteous and good at what they do. But it's difficult to get them to add something specific when they're dealing with hundreds of thousands of customers."

SUPER SUPPORT. Of course, not all shareware developers want to be your friend. Some are weekend programmers with no time or talent for pampering customers. But it's not unusual for shareware authors to man support lines personally or dispense advice by E-mail. Shareware users also benefit from a wide range of choices—from quirky niche products to alternatives to the top office applications. Say you need a tiny program that will monitor several E-mail accounts but won't hog memory and slow other programs. Instead of go-

ing to a software superstore, check out the TUCOWS shareware archive on the Net (table) and you'll find more than a dozen such programs, ranging from free to about \$30. Low marketing costs allow shareware developers to create these products, which large software companies often avoid because of slim margins.

Shareware isn't for everybody, though, and it won't likely meet all of your software needs. As Julia Pickar, an analyst with Zona Research in Redwood City, Calif., points out, download-

popular shareware programs right with leading mainstream products. the growth of the Net has led to dozens of Web sites that specialize in shareware, ranging from shareware authors' pages to vast databases such as Shareware.com. If you're not connected to the Net, you can usually order shareware directly from a developer, but you may pay a premium for the disk and shipping. Some shareware is also available on CD-ROMs packaged by software distributors.

What if you've searched the Net and come up with more than one product that might meet your needs? No problem. "Download as many as you like, try them all," advises the ASP's Holler. (Don't forget to uninstall the ones you don't want.) You may need to install some "unzipping" software first—because shareware comes in compressed and

Where's the Shareware?

**AMERICA ONLINE
SOFTWARE LIBRARY**
AOL keyword: software

CNET
www.cnet.com

FILEZ
www.filez.com

TUCOWS
www.tucows.com

WALNUT CREEK CD-ROM
www.cdrom.com
(800) 786-9907

ZDNET SOFTWARE LIBRARY
www.hotfiles.com

A huge library of files, supplemented by helpful tips, community forums, and moderated online chats.

Link from here to Shareware.com, which provides access to over 200,000 shareware files, and Download.com—a big collection of reviewed shareware and trial programs from major vendors.

Lists over 75 million files and boasts a stunningly fast search engine. Filez links to other sites that store the files. A great site for serious shareware users, a bit daunting for others.

A useful source for Internet-related software; well-organized with reviews and ratings of all listed programs.

One of the oldest shareware distributors, and one of the best for still pressing shareware CD-ROMs. Useful if you need software for an older computer.

From the publisher of *PC Magazine*; a large collection of professionally reviewed programs.

ing large applications can be a frustrating, time-consuming process. And she advises against choosing cheap shareware just to save money because of the added risk of problems with function or support. Also, some shareware programs are released in "beta," or test versions that may have serious glitches. Unless you're particularly computer-savvy, it's safest to avoid any program that has the letter "b" after its release number.

If you're still game to try some shareware, be prepared to do a little legwork, since shareware developers rarely market their programs. You'll have to sort through programs that can vary widely in quality. But doing some reading can help. Most computer magazines review

to cut downloading time—and make sure you have a good virus-checking program on your computer. For an extra measure of confidence, try some of the better shareware Web sites, such as the Net Software Library, which guarantees their shareware to be virus-free.

The bottom line: If you're looking for an alternative to that complicated database program, or a utility that does nothing but print addresses, shareware may be your best bet. Sometimes you can get more than you pay for.

By Marc Perton in New York

For reviews of popular shareware, visit BWPlus! at www.businessweek.com or on America Online at keyword: BWEnterprise

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including duties or taxes.



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Mobil

HILTON

Hertz



FELLMAN HAS STEPPED IN AS INTERIM CEO FOR 17 TROUBLED COMPANIES

WHEN IT'S TIME TO CALL A SPECIALIST

Turnaround artist Renee Fellman tells how she brings companies back to life

Business is booming? Don't call Renee Fellman. When the Portland (Ore.) turnaround specialist appears on the scene, it's almost always time for drastic measures. Over the past decade, Fellman, the owner of Interim Management Co., has stepped in as temporary CEO for 17 troubled small and midsize companies. She brought 10 of those back to health by cutting costs and firing employees and sold the others.

Her latest triumph: the turnaround of PML Microbiologicals, a family-owned firm in Tualatin, Ore., that lost \$1.5

million on sales of \$15.3 million in 1995. After 15 months under Fellman's leadership, PML was back in the black, earning \$670,000 last year on sales of \$13.3 million.

In recognition of that success, the 1997 prize for a small-company turnaround. Speaking with Staff Editor Edith Hill Updike, Fellman talked about her job, common problems faced by troubled small companies, and steps to restore an ailing company to good health.

MANAGEMENT

Turnaround Management Assn. awarded Fellman its

Q: How did you get into this special-

A: When I was in my MBA program, I knew I wanted to do consulting. I was analyzing and recommending, but I realized that once I left, a client could might or might not implement my recommendations. I wanted to do something where I could also implement.

Q: How do you usually get called?

A: Most often, I am referred either through the special assets department of a bank—"special assets" is a euphemism for troubled company—or by the company's attorney.

Are most of your clients well into crisis stage by the time you arrive?
A: Absolutely. People just don't bring anybody else in to run their company as they have serious problems. It's giving your child up for adoption.

What are the early warning signs?
A: There are many. A lack of current financial statements; payables and receivables getting older. Being placed on hold with vendors. Increasing complaints. High turnover. Constant firing. Of course, one sign all by itself doesn't mean trouble. It's multiple problems that bring companies to the brink of disaster.

How do you evaluate potential clients?
A: Ask: Is there a reasonable chance I can save this business? Is there a market for this product? Will management—and this is key—give me the authority to make needed changes?

What are the first steps? You have to get cash flowing to start, no?

A: You're right about cash. I set ground rules about what will be paid. For example, in a company in which there isn't enough money, which is the usual case, we will absolutely not pay past-due bills. Initially, we go to the bank for current products and services for current cash. To ease costs, generally the easiest ways to do are find suppliers who will negotiate at a lower cost with existing suppliers. But money-losing projects.

One of your serious business clients that simply stopped billing to credit cards almost immediately short-receivables by 60 days.

A: Yes, the management had had a marketing campaign to open accounts for everyone. It just killed their cash flow. I alerted as many people as possible about paying by credit card. For most of our customers, it was easier.

Isn't most business failure really be at the feet of management?

A: There are two primary reasons that companies get into trouble. One is poor management. The other is careless creditors. Creditors foolishly continue to lend money or provide products and

service, when, in fact, they should not.

Most of the companies I've been involved with have not established accountability within the company, and that's the major problem. I'm talking about people knowing what the company's goals are, what their jobs are—specifically, who's responsible for what, what the financial and operational targets are, and holding people accountable for achieving those results.

Q: *A turnaround usually requires some housecleaning. Presumably, you can't fire the owner.*

A: I am careful to teach my clients about what it takes to make a business run smoothly and prosper. Nonetheless, it's difficult for people who have been running their own companies to step back. [PML's] Ron Torland understood that it was time to bring in an experienced, professionally trained manager. The rest of his family, however, took months to persuade.

Q: *How do staff typically react?*

A: Initially, everyone is thrilled, because they are aware that there are problems. However, as time goes on, those—whatever their position—who are poor performers become, shall we say, dis-



Whodunit? There are two primary reasons that companies get into trouble. One is poor management. The other is careless creditors [who] continue to lend money or provide products and service when...they should not

enchant, when they discover they are expected to have a higher level of performance. Often, those people don't survive the turnaround. I have very little tolerance for incompetence and absolutely none for insubordination.

Q: *Your clients praise the quality of your recruits. How do you find people?*

A: I have a massive database. I have used my contacts, newspaper ads, and an executive search firm. I really try to keep the people who are in the company. But often that just doesn't work. Often, the really good people have left.

Q: *Who decides your exit strategy?*

A: I do everything I can not to leave until I feel that the company is on a secure enough course that it will survive. Absolutely, positively, once the new CEO is on site, I am not. You can't have two captains on the same ship. But in one situation, it took three tries. It's hard to find the right person for a troubled company, especially the smaller ones.

Q: *When do you sell vs. rescue?*

A: A key issue is whether or not the [present] management can manage the business. If not, can somebody else be brought in to run it? Once a company is financially distressed, it's very difficult to compete. So if it's in a rapidly changing industry where there's a lot of consolidation, finding a strategic buyer would be the ideal solution.

Q: *What's the personal feeling when you're done?*

A: It's almost worse than being a parent. As a parent, I felt my job was to raise my sons to be independent, and it's wonderful because even though they're now independent adults, I still have contact. When I leave a company, I don't feel I can have contact anymore

and PML is probably the best example. I just loved the people there. But we all know each other so well, that I feel I might unintentionally, by raising an eyebrow, somehow interfere with what [the new CEO] is trying to do. So it's a real loss. I have many clients who think I did a great job who would just as soon never hear from me again.

Q: *What do you do between jobs?*

A: My clients have trouble believing this, but I am every bit as good at relaxing as I am at turnarounds. I love to entertain. I love to travel. After my last project, I went to Italy for three weeks.

Q: *Any new goals for yourself now?*

A: I am already on the board of directors of one healthy company, and I'd love to do more of that. I'd like to practice some preventive medicine so that companies can avoid the kinds of situations I've had to clean up.

Join Fellman for a chat on Feb. 23 at 8 p.m. EST. Go to AOL Keyword: business dinner.



BULLIED BY BIG BROTHER? NOW YOU'VE GOT AN ALLY

A place to complain about unfair treatment by regulators

When Charles A. Garber's scientific research and materials company faced fines of \$8,000 for possible violations of Department of Transportation rules on shipping hazardous materials, he did the expected: hired a lawyer and argued to the DOT that he was exempt. At the same time, though, Garber, owner of Structure Probe Inc. in West Chester, Pa., complained to the Small Business Administration's brand-new Regulatory Fairness Program, Regfair. Its ombudsman contacted the DOT to get the facts. Soon—after Garber agreed to change his procedures—the fines were dropped. Did the inquiry help? The DOT says no; the ombudsman says probably; and Garber says absolutely. In any case, he's glad he got to vent his spleen and help the program build a record on the department's treatment of small business.

If you'd like to call your own bureaucratic nemesis to account, Regfair might be just the ticket. The program was born about a year ago, after the Small Business Regulatory Enforcement Fairness Act of 1996 directed the SBA to create a regulatory fairness ombudsman, as well as 10 regional fairness boards made up of small-business owners.

Their job is to investigate complaints and, more generally, to tell Congress whether agencies are paying attention to how their rules affect the little guy.

Ombudsman Peter Barca and his boards have devised an appraisal form business owners can file—anonously, if they wish—about either enforcement actions or specific regulators. In the past year, they've heard cases such as these:

■ Albuquerque restaurateur Kathy Diaz claimed an Internal Revenue Service agent subjected her to a "five-year reign of terror" that began when the agent scrapped a back-taxes payment agree-

ment reached with his predecessor. According to Diaz, the agent was so angry about her testimony before a regional fairness board that he threatened to seize her business. She complained to IRS higher-ups, who ultimately put another agent on the case. (The IRS declined to comment.)

■ Joyce Chen Inc., a 23-employee kitchen products company, said it got caught in a turf conflict between the Environmental Protection Agency and the Food & Drug Administration. The company's lawyer, Michael Morizio, says Joyce Chen's antibacterial cutting board won FDA approval—but then was derailed by the EPA to halt production because of a question about the labeling of a pesticide used in the board. After months of negotiations, the company has reached an agreement and is paying off \$82,500 in fines.

The SBA didn't help resolve these cases. Indeed, Barca says it's not his job to intervene in specific enforcement actions. So why complain to an office that can jawbone but has no teeth? Because, backers say, Barca can alert Congress the same agency comes up repeatedly. "No agency wants to be recognized as the worst small-business agency in government today," he says. (So far, the IRS and the EPA lead the unpopular contest.) Barca is under pressure to get tougher by some on Capitol Hill, including Senator Christopher S. Bond (R-Mo.), chairman of the Senate Small Business Committee, who wrote the Regfair law. Bond wants to avoid finger-pointing to be

REGULATION

specific and aggressive.

Members of regional fairness boards, meanwhile, urge complainants to get their pain. "We have an opportunity to really refine the regulatory process," says mid-Atlantic board member Sam Marcell, owner of Prima Facie Inc., a telemarketing research company in King of Prussia, Pa. He calls the first year a "baby's first time." Now, he says, the boards are ready to roll, and interest is picking up. Some 20 new complaints were filed in the past four weeks (33 came in during the previous year) and Barca is asking for more staff to keep up with the calls.

So if you want to take Washington, here's a place to start. It can't hurt; it might just help. But as Garber, Diaz, or Morizio would tell you, don't fire your lawyer just yet.

By Linda Stern in Washington

THE COMPLAINT BOX

Got a gripe with the feds? Speak up if you think you've been treated unfairly

• **WHO'S IN CHARGE?** The Small Business Administration has created a new position of ombudsman who oversees 10 regional fairness boards made up of small-business owners. Former Congressman Peter Barca holds the post.

• **WHY COMPLAIN?** The ombudsman and boards take complaints, check them out, and report to Congress on how regulators treat small business. The investigation might spur an agency to act, and the attention could forestall future problems.

• **HOW DO YOU FILE?** Call 888-REG-FAIR, or surf to www.sba.gov/regfair on the Web.

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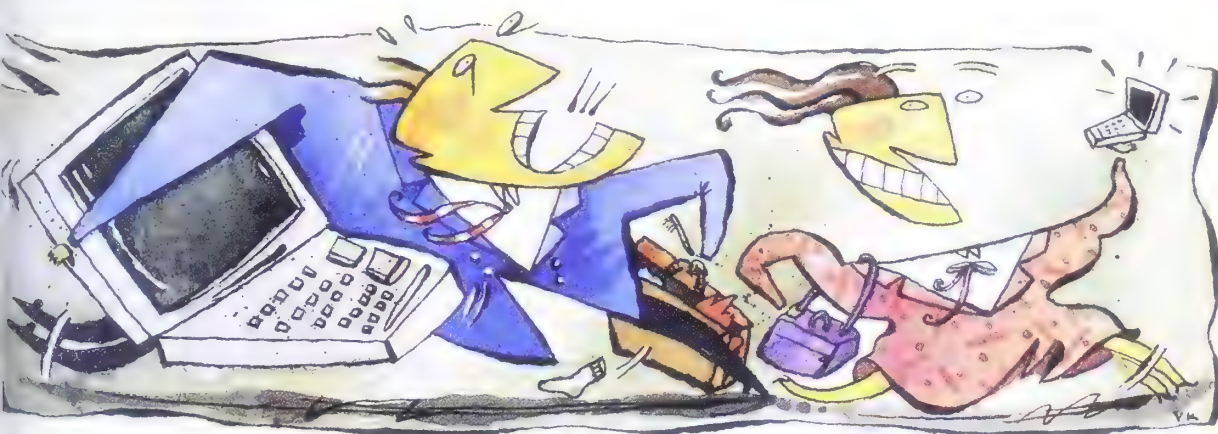


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When suppliers schmooze with Kurt Krempa of Olson & Terzian P. C., an engineering design firm in Buffalo, it's usually over lunch. Occasionally it'll be during dinner or golf. But two years ago, he was entertained as never before.

Deborah Naybor, owner of a land-surveying company, taught Krempa and his family to scuba dive. He was especially impressed at how Naybor talked his claustrophobic cousin through her fear of murky Lake Erie. "We now have a personal relationship," Krempa says. "That takes much longer to develop through lunches."

Introducing '90s-style business entertaining: It's more creative and varied than ever. Impressing clients can be as simple as a family dinner at home or as elaborate as a cruise with a jazz band. Such events are as tax deductible as any other business entertainment: generally 50% to 80%, minus the cost of nonbusiness-related guests, such as spouses.

The shift is due in part to new demographics. Women and Gen-Xers are less likely to enjoy pastimes such as golf, steak dinners, or, at the extreme, strip joints. It also reflects a new national focus on health and family. "Entertaining has become more a marketing tool and less a perk," says John Cebrowski, a marketing professor at Pace University's World Trade Institute.

Developing personal relationships is particularly important for small businesses. "I am the business," says Donna Hegdahl, a marketing consultant in Dallas who has taken clients to yoga

DOWN TIME

Not Necessarily Out to Lunch

ENTERTAINING CLIENTS IN THE '90s IS LESS PREDICTABLE AND MORE PERSONAL



OM WORK: Donna Hegdahl (L) took client Julie Addicott to yoga class

class. "I try to be a resource to their whole life."

Observers say these new styles stem partly from how women work. "One thing they do more than men is network clients," says Edith Weiner, co-author of *Office Biology*, a book on workplace trends. Susan Stautberg, whose New York-based PartnerCom helps

GEN-X EFFECT:
The shift is due in part to new demographics

companies form advisory boards, invites associates, mostly women, to her home periodically to meet a featured guest, such as a fashion designer or a politician.

Group recreation can do double duty, depending on the guest list. Outings that include spouses and children can help develop deeper relationships with clients. And bringing prospects along to mingle with established customers gives them a chance to learn firsthand about the host's business.

Not that old-style entertaining is dead. Women are taking up golf and cigars; martinis are making a comeback. But people are no

longer limited to the old standards. For some, entertaining in athletic activities beats watching them from the skybox. In Denver, small companies often take clients rock climbing or skiing. Don Price, marketing guru at the local Small Business Development Center.

New-style entertaining can have hidden benefits. When consultant Hegdahl took Julie Addicott, a marketing manager at GTE Communications Corp., to her yoga class, the pair said they felt so relaxed the

were more productive brainstorm afterward. Art Kosatka, an air security consultant and amateur pilot, the Washington area, takes clients flying. "The spectacular scenery over D.C. makes quite an impression," he notes. "Then we have a burger at the airport in the sky. No distractions, we can talk freely."

ART CIRCUIT. Many people appreciate activities that have value, either personal or professional, to the fun. Yeager, a law partner in Washington, took a business associate who was

furnishing a house to a tiques show. Others say clients enjoy museum exhibits and art lectures. Inviting clients and their employees to do charity work can create a special bond, too. "Doing a clothing or food drive gives my clients a chance to meet their friends when they go pick up goods," says the land-surveyor Naybor.

So think out of the box, the skybox, that is. By building relationships with personal touch, business owners can enrich themselves in more ways than one.

By Edith Hill
in New York

THIS COLLAR GOES TO FILEMAKER PRO.

The Town of Poughkeepsie Police Department uses FileMaker Pro to organize their entire operation. So they can nab more bad guys.

The Town of Poughkeepsie Police Department once used two pads and a ballpoint pen to track cases. Though this is a common system, it leaves a lot of holes. So with no formal software training at all, Detective David Lundgren entered a new and better way. He rounded up some drug-seizure money, picked up a copy of FileMaker® Pro software, and quietly revolutionized his department's operations.

MILIONS OF FANATIC USERS

If you think the Town of Poughkeepsie PD is an isolated case, your evidence must have been tampered with. Truth is, millions of zealous users in organizations of all shapes and sizes manage their data with FileMaker Pro. It brings new information to light, you can customize it to the way you work, and it's easy to use. Importing spreadsheet data is as simple as dragging and dropping.

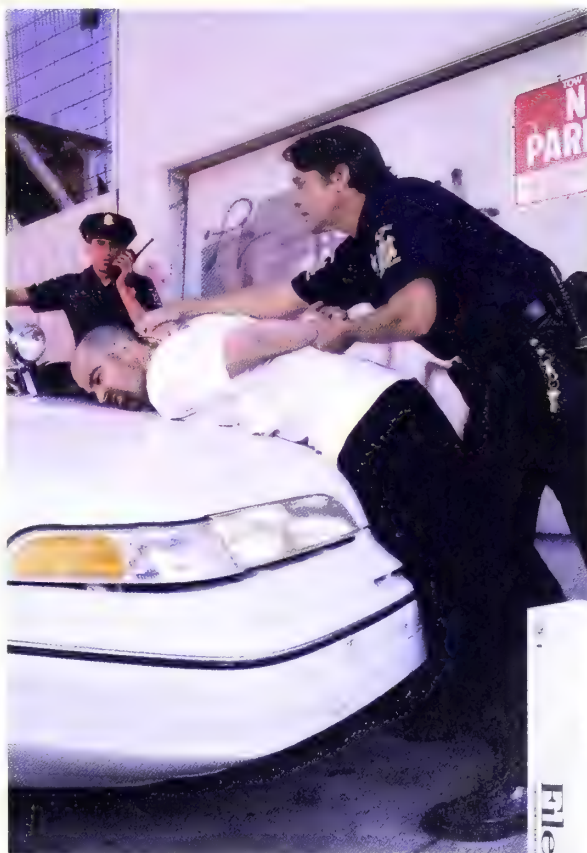
MANAGING INFORMATION IS A SNAP

Ask Detective Lundgren: Yesterday we brought in a suspect for a string of residential burglaries. The detective did a quick find on his laptop: burglaries in Zone 2 since August.' The suspect confessed to five of them. And there's no way we would have if we hadn't had FileMaker Pro."

USE INFORMATION IN WAYS YOU NEVER THOUGHT POSSIBLE

FileMaker Pro can show you information you didn't even know you had. And its extensive sorting and reporting capabilities let you view that data however you like, creating everything from simple mailing labels to a complex inventory system. Spreadsheets just can't do that. What's more, anyone can use it. "I have guys working for me who can erase a hard drive just by looking at it," said Lundgren, "but every one of them gets the job done with FileMaker Pro."

To get the full story on how FileMaker Pro has simplified life for the Town of Poughkeepsie PD and other organizations, visit us at www.filemaker.com/bwe. Or visit your local reseller so you can start using FileMaker Pro right now.



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THE INTERNET

PORTAL COMBAT COMES TO THE NET

Why all those online heavy-hitters want to be your doorman

Microsoft Corp.'s 10 Web sites are among the biggest draws on the Internet, visited by a third of all U.S. Web surfers. Yet it's not enough. So the software giant is jacking up a super Web site that will weave all its online properties, from travel to car-buying to news, and include services such as free E-mail and a search engine to explore the rest of the Web. The new site, which could be ready as early as this summer, will be called "Microsoft Start"—a telling name, since the software maker is hoping all these goodies will persuade cybernauts to make it their first stop on the Net.

It's home sweet home page. And Microsoft isn't the only business trying to create the best one. Yahoo!, CNET's Snap! Online, Excite, Netscape, and half a dozen others are making bids to become the launchpad to the rest of the Net. They are jamming their Web sites chock-full of free services—chat, customized news pages, entertainment listings, even personal finance advice—hoping Netizens will visit them first to get most of the stuff they need.

The theory: If a Web site becomes a major gateway to the Net, or "portal," it will boast traffic from a big chunk of the 55 million Web surfers. That could

draw advertising dollars, online shoppers, and lucrative sponsorship deals, transforming money-losing sites into cash machines. The prize is huge: Advertising on the Net is expected to hit \$7.7 billion by 2002, up from \$940 million in 1997, and E-commerce could balloon to \$37.5 billion, up from \$2.6 billion last year, according to market researcher Jupiter Communications Co. "It's hard to find any of the major sites that aren't seeking to be the start site," says Laura Jennings, vice-president at Microsoft Network, the No. 2 online service.

The idea of portals marks the latest twist in the Web's evolution. A year

Information Technology

ago, search-engine sites such as Yahoo! and Lycos feared they would become commodities. So they began touting themselves as newfangled "networks" that—much as in the TV world—would act as channels funneling programs, information, and news to subscribers. Now, they and other ambitious Web-site operators are taking it further, attempting to become one-stop, full-service sites.

And none is more successful at it today than America Online Inc. AOL is the No. 1 doorway to the Net, with its 11 million subscribers accounting for a hefty 39% of Web traffic, according to Media Metrix-The PC Meter Co. AOL's oodles of content, shopping, chat, and E-mail have drawn hordes to the proprietary online service. Now AOL is beefing up its Web site, AOL.com, to ward

cite Inc., Yahoo! Inc., and others are piling on services that are being matched almost instantly by rivals. Last October, for example, Excite paid \$35 million in stock for Netbot Inc., which developed an online shopping technology that helps find products across a welter of Web merchants. But before Excite could launch the shopping service on Nov. 26, Yahoo! trumped it by unveiling a similar comparison-shopping feature through a licensing deal with Junglee Corp. of Sunnyvale, Calif.

The latest must-add feature: online communities. These let Web surfers homestead by setting up their own pages around common interests. "Neighbors" chat online and exchange information on topics ranging from Southern living to Broadway. Yahoo! kicked that off in January by taking a \$5 mil-

vice-president of business operations. Yahoo!

It's also getting more expensive by the day. Take Yahoo!, which licensed search service two years ago and developed features in-house before buying additional ones in the past year—a total cost of \$205.5 million. To recreate that same service from the ground up today would cost between \$500 million and \$1 billion, analysts say. "The separation between the haves and the have-nots will begin in earnest in 1998," says analyst Mary G. Meeker of Morgan Stanley, Dean Witter, Discover & Co. **BULKING UP.** So, too, will the pace of acquisitions, as the "haves" bulk up with extra features and make a grab for subscribers, figuring they don't have much time left to get established. One likely buyout candidate, say analysts,

Bigger, Better, Faster

COMPANY	FEATURES	PERCENT OF USERS' VISITS	
		HOME	WORK
AOL.COM	Offers a link to the Internet for AOL's 11 million subscribers, with loads of content, E-mail, news, and chat	46 %	41 %
YAHOO! SITES	A top Web brand that's setting the pace for new features—such as free E-mail, chat, local listings, customized Web pages	42	51
MICROSOFT SITES	Building a supersite called Microsoft Start that will tie together all its properties in travel, personal finance, games, news, and car buying	33	40
EXCITE NETWORK	Signing exclusive deals with companies such as Intuit to offer financial services and investment information	24	30
WALT DISNEY SITES	Using its stable of properties—Mickey Mouse, ESPN sports, ABC entertainment and news—to draw a wide audience, including kids and sports buffs	14	12
CNET NETWORK	Tops in technology news and software sites, it's now branching out by licensing its Snap! service, a collection of content with search and chat	11	13

DATA: MEDIA METRIX, THE PC METER CO.

off the portal wannabes. Its site offers features once only available on the online service, such as instant messaging—a real-time E-mail exchange much like chat—and NetMail, which lets AOL users check E-mail from the Web without having to use the AOL service.

PILING ON. So far, it's paying off. AOL's revenue from advertising, goods, and services sold electronically rose to \$108.8 million in the December quarter, up 87% from a year ago. But AOL is facing stiffer competition. CNET Inc., for example, is muscling in by licensing Snap!—a collection of Web content created by others—to such biggies as Toshiba, CTE, and Compaq Computer. "Our bet," says Halsey M. Minor, chief executive at CNET, "is that everybody combined will be able to generate more customers than AOL."

But first, CNET and the others must outdo the online giant—a task that's triggering an all-out features war. Ex-

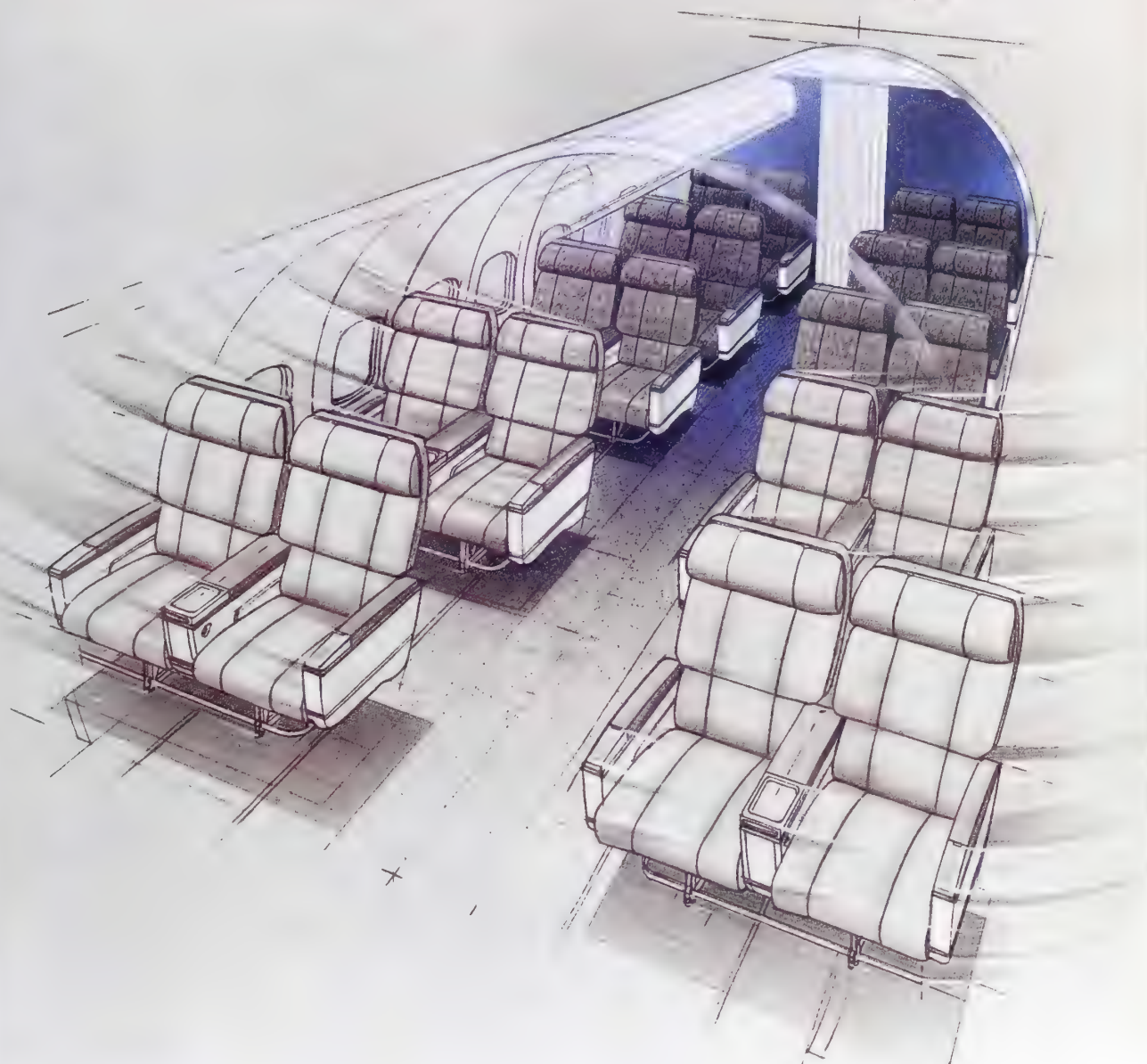
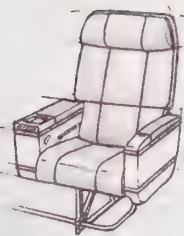
lusion minority stake in GeoCities, a privately owned Santa Monica (Calif.) online community that was ranked the seventh most popular site, according to RelevantKnowledge Inc. Lycos Inc. followed by acquiring Tripod Inc. on Feb. 3 for \$58 million in stock. The Web community for twentysomethings boasts 1 million members. Now, AOL says it's considering a similar service. "This space is very unforgiving because your competition is one click away," says Jeff Mallett,

They're filling their sites with freebies to make them a surfer's first stop

Mirabilis Ltd., an Israeli startup that has developed real-time chat now used by 4 million people. Also attracting WhoWhere? Inc., a Mountain View (Calif.) company that provides free e-mail and was the 15th most popular site in January. Experts also bet iVillage will be snapped up soon. The New York-based company, which owns the popular Parentsoup site, is one of the top 10 communities, with 2 million monthly users, offering information targeted to women on finance, parenting, and work. Co-founder Candice Carpenter says iVillage has been approached by media companies, though she won't name them. "We've had inquiries, and it's speeding up," she says. "This is in the air."

So who will be standing when the portal combat is over? Experts say there will be four major doorways to the Net, maybe six—including AOL, Yahoo!, and Microsoft, which are sitting pretty with the most traffic and a

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Steve Burgile, Vice President - Business Systems, The Earthgrains Company



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deepest pockets. Experts say Excite and media companies such as Time Warner or Disney—which is starting to put its gateway pieces together—will duke it out for the other spots.

The smaller players, such as Lycos, which had 18 million daily page views in the latest quarter, and Infoseek, with 12.5 million, need to partner up, says analyst Alan M. Braverman of Credit

Suisse First Boston. That's because their numbers—and ability to attract advertisers—are dwarfed by the 65 million page views and the breadth of the services Yahoo! is putting together. Infoseek executives decline comment about a partnership, saying they are in a quiet period after a secondary stock offering. Lycos, which turned profitable in the October quarter, says partners have

indicated interest in the startup. But says CEO Robert J. Davis, "we're completely committed to growing as an independent company."

The way the competition is shaping up, even small fry can leverage the success of the biggies to draw a crowd.

By Heather Green in New York and Linda Himelstein in San Francisco with Paul C. Judge in Boston

THE WONDERFUL WORLD OF DISNEY.COM

No one loves brand names more than Michael D. Eisner. Whether it's the *Beauty and the Beast* Broadway show that kids drag their parents to or the new ESPN store that lures sports nuts to a shopping mall in Glendale, Calif., the Disney chairman has long preached that the best way to draw a crowd is to give them something they'll recognize in a crowd. It should be the same on the Internet.

Certainly, that's the mantra at Walt Disney Co.'s online unit, Buena Vista Internet Services. As Web usage, advertising, and E-commerce catch on, so too has Disney's interest in carving out a piece of the Internet pie. Indeed, the company has been in talks to buy the remaining two-thirds it doesn't already own of Web-site owner and designer Starwave Corp., say insiders. Starwave, which operates the popular ESPN SportsZone and Mr. Showbiz sites, would give Disney a key property that would help tie together a collection of two dozen sites aimed at doing what Disney does best—entertainment.

PUSHING POOH GRAMS. No major media company is more aggressively pushing to cash in on the Web than Disney, whose online expenditures were an estimated \$150 million in the last year alone. As many as 25% of Netizens visit at least one of the Disney sites each month, whether to send "PooH grams" or to "own" one of the 100,000 or so football, basketball, or baseball teams that compete in ESPN SportsZone's fantasy leagues.

Disney has the combination of technical savvy, brand name, and deep pockets it takes to compete. Working out of a six-floor office building in North Hollywood, many of its 300 artists, writers, and programmers create as much new Web content as any company in the industry. To get the technical expertise it lacked, Disney plunked down an estimated \$80 million last April for one-third of Starwave, which was launched by Microsoft Corp. co-founder Paul Allen. "They're aggres-

sive, and they have a lot of resources," says Scott Webb, senior vice-president of Viacom Inc.'s Nickelodeon Media Works.

Disney is pulling all its strings to make a profit on its money-losing Net operations. It generates healthy distribution fees from America Online Inc., which features its ABCnews.com site. Its sites take in an estimated \$25 million a year in ad revenues. And www.Disney.com sells some \$8 million in trinkets. The company also boasts an estimated 70,000

members at \$5.95 a month to its 10-month old Disney's Daily Blast service for kids. Can Disney's Web sites keep the rivals at bay? The kiddie sites have heavy competition from the likes of AOL, Warner Brothers and Nickelodeon. Disney's ABCnews.com is No. 4 in news. And even ESPN, which handily leads all sports sites, faces mounting competition from CNN/SI and CBS's SportsLine. Still, among the media industry's best marketers, Disney has an arsenal of

promotional tools that includes its theme parks, movies, TV shows and even its Mighty Ducks hockey team. For instance, the company slipped promotions for the Daily Blast into 8 million copies of *George of the Jungle* videocassettes, and will soon pitch the service at the Innovations booth at Epcot Center.

Down the road, the company sees its place in the world of convergence, with ESPN offering online sports statistics for the cable channel

or www.Disney.com offering a quick way to buy products that a kid might see in a movie on ABC's *Wonderful World of Disney*. "The companies that will win on the Internet are those who have the ability to create content, and no one does that better than we do," says Jake Winebaum, Buena Vista's president. But in the hotly competitive Web world, Disney may need some Tin-kerbell dust, too.

By Ronald Grove in North Hollywood, Calif.



WINEBAUM: *The winners "are those who create content"*



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THE ASIAN CRISIS

THE SWAT TEAM FROM WASHINGTON

Now a trio from Treasury is helping to contain the damage

David A. Lipton is getting his 15 minutes of fame—but only at the dry cleaners. Lipton, Treasury Under Secretary for International Affairs, flew to Seoul before Christmas on a delicate mission: meet face-to-face with president-elect Kim Dae Jung to gauge commitment to the harsh reforms demanded by the U.S. and the International Monetary Fund before Korea got lions in new aid. In Korea, Lipton's act was front-page news and a hot topic on TV. In the U.S., he was an invisible man until he dropped his laundry off. "I saw you on TV," said the clerk at his neighborhood cleaners who caught him on Korean cable network. "You're famous!" Not much buzz for the 44-year-old Lip-

ton, one of the lead negotiators in talks with Thailand, Korea, Japan, and the other nations at the center of the biggest global financial crisis of the decade. But like the rest of the Treasury bailout team led by Deputy Secretary Lawrence H. Summers, Lipton doesn't have time for the fame. If U.S. policy is ultimately successful in helping stem the crisis, much of the credit should go to Summers, Lipton, and Assistant Secretary for International Affairs Timothy F. Geithner. Of course, if the crisis spins out of control, they may well have to shoulder the blame.

How Summers, Lipton, and Geithner manage the latest brushfire in Indonesia could determine whether the trouble spreads to Latin American and Russia.

SUMMERS, LIPTON, AND GEITHNER:

Some critics say they've imposed unwarranted austerity measures

On Feb. 17, they were again confronted with a crisis as President Suharto, intent on pegging the rupiah to the U.S. dollar, dismissed his central bank chief, who accused him of reneging on reforms and imperiling a \$40 billion IMF bailout. As one Hong Kong official says of Summers: "The more he builds up his image as a white knight saving Asia, the more he'll have to deal with the consequences [if things go wrong]."

Because the U.S. is technically just following the IMF's lead, Summers & Co. have to alternate between pressure and prodding to move toward a consensus—and they have to be fast on their feet. In January, for example, during one of the scariest moments in the Asian crisis, the three worked the phones for two weeks to keep bankers and Korean negotiators on track as they struggled to stretch out \$24 billion in loans owed by Seoul—and avoid a banking-system meltdown that might have spread to the rest of Asia. The behind-the-scenes maneuvering worked: On Jan. 28, the banks granted Korea a three-year reprieve on the debt. Most Asian equity and currency markets have climbed steadily ever since.

GRUELING. That scare was handled long distance, but usually the travel alone makes for a grueling job. During Geithner's sixth trip to Asia since August, his wife jokingly asked officials to post his picture on the Treasury's Web site so she could remember what he looked like. In a seven-country blitz in January, Summers and his deputies implored the Indonesians and Koreans to stick with reforms, encouraged the Chinese to resist a currency devaluation, and tried to soothe Thai officials incensed over Congress' refusal to contribute to their bailout.

As leader of the trio, Summers, 43, a former Harvard professor and World Bank chief economist, can be eloquently persuasive with foreign leaders, but he also has a brusque, headstrong style that has prompted several senior Treasury careerists to take early retirement. Lipton and Geithner, say colleagues, have the intellect and moxie to joust with their boss.

The son of a Ford Foundation execu-

ECONOMIC TROUBLESHOOTERS

LARRY SUMMERS

Deputy Treasury Secretary, Age 43
Brilliant, abrasive, workaholic. Former star at Harvard and the World Bank. Joint man in the Asian crisis.

DAVID LIPTON

Under Secretary, Age 44
Former IMF economist and consultant, helped Poland and Russia open up markets. Self-effacing, but stern.

TIMOTHY GEITHNER

Assistant Secretary, Age 36
The guy with the cultural smarts about Asia, thanks to a childhood spent partly in India, Thailand, and China.

Government

tive, the 36-year-old Geithner grew up in Rhodesia, Zambia, India, Thailand, and China before joining Treasury's Tokyo office in 1990. There, he won credit for helping to persuade Japan to pony up a \$13 billion donation for the Persian Gulf war and to open its markets to U.S. financial-services firms. His acumen came in handy last fall when Japan proposed an Asia Fund, bankrolled by the region's rich countries, to bail out troubled economies. The idea of Japan dominating such a potentially powerful institution wouldn't sit well with smaller Asian nations, Geithner figured. So he used those concerns to help beat back the plan. "He understands Asian sensitivities, which is quite unusual for an American," says Japan's Vice-Minister for International Finance Eisuke Sakakibara.

Lipton, a Boston native and Harvard classmate of Summers, spent eight years as a staff economist at the IMF and then two years as a private consultant advising Russian and Polish officials on how to make the switch from socialism to capitalism. And at Treasury, Summers and Lipton oversaw the \$55 billion rescue of Mexico, widely seen as a success. "He's the best 'country doctor' I know," says

his predecessor, Jeffrey R. Shafer, now vice-chairman of Salomon Smith Barney International Inc. "He's a pragmatist who has no interest in debating theoretical points." Adds Summers: "David understands the intricacies of the IMF programs so well he can help the IMF build their spreadsheets from the bottom up."

Maybe that's why Lipton relaxes by watching action flicks: "If someone doesn't die by the opening credits, I'm bored,"

Treasury Secretary Robert Rubin says his aides are "schooled in the international language" of crisis management

he's told friends. While Lipton won't discuss his role in the initial talks between Korea and the IMF, Seoul officials say he was an integral player. The Koreans say the IMF's chief negotiator kept adding conditions after phoning or meeting with Lipton. Korean papers painted Lipton in even darker tones, portraying him as a heartless manipulator of the talks.

Summers and his colleagues have plen-

ty of detractors, from congressional isolationists to foreign leaders who resent the heavy hand of the U.S. The Treasury team is "primarily representing U.S. interests," says Park Yung Chul, president of the Korea Institute of Finance, a government-affiliated think tank. "They could have contained the problem in Thailand before it developed into a full Asian crisis. But they didn't." Ironically, one of the most vocal detractors is Lipton's former consulting partner, Harvard international economist Jeffrey Sachs, who thinks Treasury and the IMF are pushing austerity measures at the very moment Asia needs stimulus.

Summers and colleagues point out no one has come up with any better ideas for the crisis. "We're at the frontier of so many issues," notes Geithner. "There's no road map."

And there's no telling when a rescue package like Indonesia's might begin to topple. As the Summers squad rushes to that emergency, there was only one certainty: A new round of exhausting behind-the-scenes maneuvering lay ahead.

By Dean Foust in Washington, William Moon Ihwan in Seoul, Joyce Barnath in Hong Kong, Patricia Kranz in Moscow, and bureau reports

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DICK CHENEY AIN'T STUDYIN' WAR NO MORE

As an Iraq attack seems nearer, he's in a far quieter oil patch as CEO at Halliburton

Dick Cheney is best known as a seasoned cold warrior. So, as the U.N.'s war of words with Iraq flares up, the former Defense Secretary and Persian Gulf war strategist is once again a hot media commodity. CNN wants his take on the sorry state of the Persian Gulf war coalition. *USA Today* wonders if he's running for President in 2000. As cool, composed, and cerebral as he was at the height of the 1991 crisis, Cheney smoothly fields all the queries. Only this time, he's handling them from his big corner office at Halliburton Co., the oil-services giant.

It seems an unlikely venue. But Richard B. Cheney, conservative pol and 25-year Washington veteran, has been learning a new career as CEO of the \$9 billion Dallas-based Halliburton. And since taking over in 1995 amidst a global oil boom, he has made the transition to corporate life with apparent ease. But the real test of management skills will come with the inevitable oil downturn. That's when he will have to prove he's more than a big-name executive with a golden Rolodex. **SMART WELLS.** For now, though, Cheney is hard at work shifting Halliburton into high gear. He's well on the way to transforming a low-tech, old-fashioned oil-services company into a leader in so-called "smart" wells. — *Forbes* Cheney uses computer software and magnetic imaging to help identify rich deposits. Already, Cheney has poured more than \$1 billion into such technologies. At the same



GLOBAL CONTACTS

"Dick gives us a level of access that I doubt anyone else in the oil sector can duplicate," says David Lesar, president of Halliburton

time, he's courting politicians and business leaders through the booming Caspian Sea region in an all-out effort to secure key political ties with Azerbaijan and Kazakhstan. Accounting for the world's third-largest oil reserves, the region is Cheney's best hope to secure big contracts for a long time to come.

In Halliburton's two years under Cheney, it has clearly prospered. With demand for its sophisticated offerings soaring, profits jumped an eye-popping 51% last year, to \$454 million, sending

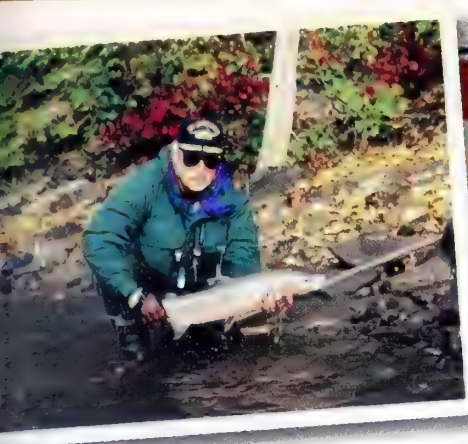
shares up 72%—among the best gains in the patch. And in 1998, profits should climb another 30%, according to Zacks Investment Research. The pay sure beats government work, too. Cheney earned \$2.2 million salary and bonus and picked up stock options worth \$10 million.

BIG BITE. In an era when tycoons spend their millions in pursuit of electoral office, Cheney is more in the opposite direction. Born in Nebraska and raised in Casper, Wyo., he's a mix of avid outdoorsman and quiet intellectual. Friends say he's relaxed in jeans, cowboy boots, and cap as he leaves the corporate jet. But they note that on fishing trips he'll keep a large book burning late into the night, reading military history.

It was on one such trip that Cheney crossed paths with former Halliburton Chief Executive Thomas H. Cruikshank. On a 1994 fishing trip in British Columbia with several CEOs, his fireside chat of restructuring the company convinced Cruikshank

that, a year later, he offered to replace Cheney. "There are more synergies than people would think between running the Pentagon and running a corporation," says Cruikshank.

As was his style in Washington, Cheney is not charging in to force his agenda on Halliburton. Instead, he focuses on setting the strategic agenda while his top managers free rein to pursue a series of high-tech acquisitions. "There are a lot of people here who know more about this business than I do," he says.



His wife says Cheney loves fly-fishing more for "all the preparation" than the actual experience itself

STEELHEAD IN HAND

Meanwhile, he has concentrated on building Halliburton's international profile through a network of contacts developed during his Washington days. Indeed, Cheney's business and social worlds blur together in a whirlwind of travel, meetings, and parties. Recently, for instance, Cheney, 57, and his wife, Lynne, a senior fellow at the American Enterprise Institute, were among the guests saluting Saudi Arabia's Prince Bandar and his wife on their wedding anniversary. Bandar, longtime ambassador to the U.S., is also a nephew to King Fahd. Says Halliburton President David J. Lesar: "Dick gives us a level of access that I doubt anyone in the oil sector can duplicate."

POND. The company won't reveal to what extent Cheney's contacts have helped in new business. And given the time required to develop projects, it's too soon to tell whether Cheney's making will succeed. But there's no question he has helped catapult the company into the big leagues. In the Caspian area, he has brought the relatively small Halliburton into an exclusive circle of major oil companies. Together with the heads of Chevron Corp. and Texaco, Cheney is one of just a dozen members of Kazakhstan's Oil Advisory Board, created by the country's president as a guiding board. "His name and stature at Halliburton much greater opportunities," says Victor G. Beghini, CEO of company Marathon Group.

In the high-stakes world of oil geopolitics is a long way away from Cheney's Western roots. As a boy, he learned to read books as much as the outdoors. When Cheney was 13, his family moved from Wyoming to Nebraska. In Casper, Cheney made the local library his summer hangout, poring over thick history books. A standout athlete and student in high school, he earned a full scholarship to Yale University. There, though, the young Cheney was overwhelmed by academic rigors and wound up flunking out. "I had a lack of direction, but I had a good time," Cheney now recalls. Back in Casper, Cheney went to work

for the local power company, climbing poles and setting lines. That was enough to convince him to take another shot at college. This time he enrolled in the University of Wyoming, paying \$96 a semester in tuition. After earning a master's degree in political science, he received a congressional fellowship.

Once in Washington, Cheney caught the eye of Congressman Donald H. Rumsfeld (R-Ill.), who was impressed with his hard work and discipline. Rumsfeld brought his protégé with him to the Nixon and Ford Administrations,

RICHARD B. CHENEY

BORN Lincoln, Neb., 1941
Raised in Wyoming

EDUCATION B.A. Univ. of Wyoming, 1965; M.A. 1966

CAREER

1969-74 White House aide

1975-76 Chief of Staff to President Gerald Ford

1978-89 U.S. Representative from Wyoming

1989-92 Defense Secretary

1995-present CEO, Halliburton

BIGGEST ACCOMPLISHMENT

Built global coalition to push Saddam Hussein out of Kuwait in the Persian Gulf war, 1991

FAMILY Married to Lynne Cheney, senior fellow at the American Enterprise Institute; two grown daughters

INTERESTS History, military strategy, fly-fishing, skiing, hunting

and when Rumsfeld went off to run the Pentagon, Cheney took over as Ford's chief of staff at age 34—the youngest ever to hold the job. After Ford lost the 1976 election, Cheney got himself elected congressman. In 10 years in the House, he carved out a specialty in foreign affairs and chucked up a conservative voting record that rivaled Senator Jesse Helms's. In 1989, he was plucked to run the Defense Dept.

At the Pentagon, Cheney oversaw a massive military restructuring, dwarfing anything seen at IBM or AT&T. With the end of the cold war, he and his staff reoriented the military toward regional rather than global conflicts. The decision paved the way for the painful 25% reduction of the Pentagon's forces, the closing of 800 bases around the world, and billion-dollar reductions in defense budgets.

Quiet, intense, and at times brusque, Cheney avoids small talk on the job, even with his oldest buddies. David Gribben, Halliburton's vice-president for corporate affairs, who has known Cheney since high school, says meetings last only until he can get the boss's approval. One business friend calls him The Sphinx, says Lynne Cheney. At the Pentagon, his poker face earned him the nickname Deadpan Dick. Even Cheney's hobbies are an exercise in discipline. His wife says Cheney loves fly-fishing more for "all the preparation that goes into it" than for the actual experience.

STAYING PUT. Given the challenge of positioning Halliburton for the unavoidable industry downturn, his methodical approach will come in handy. In 1996, Cheney paid \$560 million for Landmark Graphics Corp., a company with data-analysis tools that help puzzle out all the pieces of seismic surveys. A bigger acquisition, however, could be in the works. Many industry experts suspect that Cheney is eyeing Western Atlas Inc., a seismic services company currently valued at \$3.8 billion. While he plays down talk of the deal, Cheney doesn't rule it out.

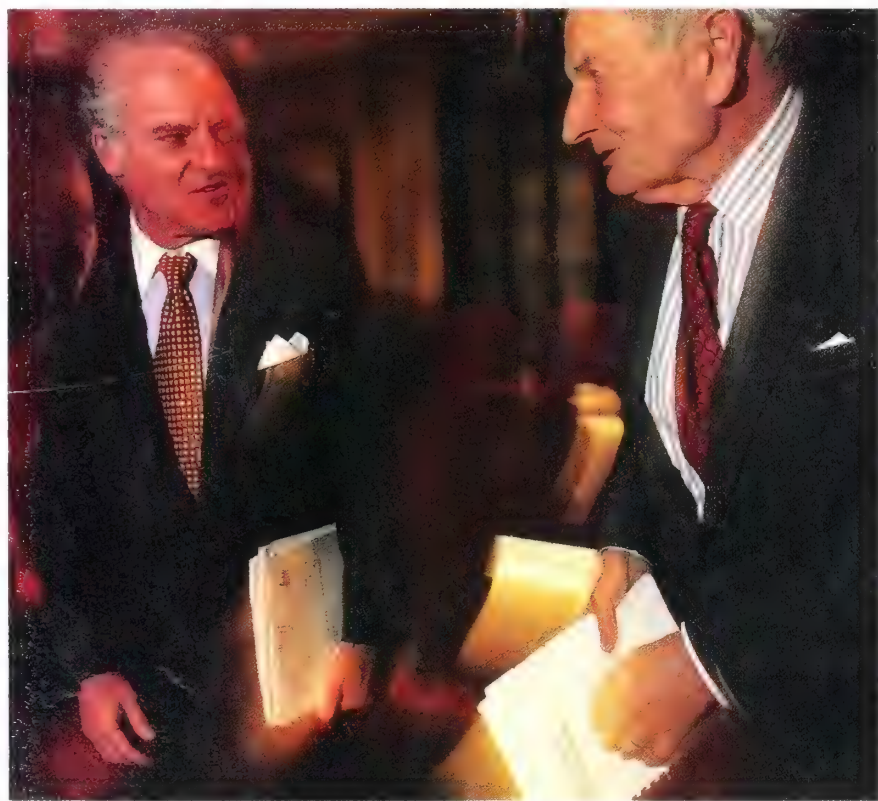
If Cheney is coy about a bid for Western Atlas, he is perfectly clear about one point: He won't be making any bids for elected office anytime soon. Although friends point out that he still stays in touch with former President George Bush and White House colleagues James A. Baker III and Colin Powell, Cheney insists that's as far as it goes. "This is where I expect to spend the rest of my career," he says. With the oil market booming and CNN and USA Today still hanging on his every word, it seems that Cheney is sitting pretty right where he is.

By Gary McWilliams in Dallas

CITIES

HENRY KRAVIS ... DO-GOODER?

The LBO king is raising millions for inner city NYC



Works in Progress

Some of the New York City Investment Fund's projects:

	INVESTMENT MILLIONS	CHAMPION	NEW JOBS	COMMENTS
PARTNERSHIP PLAZA	\$2.50	David Komansky, CEO, Merrill Lynch	1000	Building six inner city shopping strips
ROYAL HEALTH CARE	2.00	Russell Carson, partner, Welch, Carson, Anderson & Stowe; Jeffrey Krauss, partner, Nazem & Co.	850	Medicaid managed care organization at two hospitals, in Brooklyn and Queens
SHOOTING GALLERY	1.50	Michael Lobdell, managing director, J.P. Morgan	250	Film production center in lower Manhattan
ERICSSON CYBERLAB EAST	0.75	Ed Horowitz, Citicorp; Clifford Friedman, Bear Stearns	10	Product-testing lab in Manhattan for New York's Internet industry

SOURCE: NEW YORK CITY INVESTMENT FUND

Van Deward Woods, owner of Sylvia's Restaurant, a popular Harlem soul food eatery, and billionaire Henry R. Kravis do have much in common. Woods, son of founder Sylvia Woods, serves up fried chicken and ribs on a gritty Lenox Avenue block where street vendors blare rap music. The offices of Kravis' firm, Kohlberg Kravis Roberts & Co., sit above tony West 57th Street, offering dazzling views of Central Park.

Their lives, however, have become curiously entwined. Kravis' creation, the New York City Investment Fund, has dedicated a team of executives, led by former Liz Claiborne Chief Executive Jerome A. Chazen, to consider any investment in Sylvia's. The fund also introduced Woods to key food company executives to provide strategic advice about expanding his company, possibly putting Sylvia's canned collard greens and yams in supermarkets nationwide and bringing jobs to Harlem. "To me, the chief executive of one of the largest food companies in the world..." African-American entrepreneur marvels. "It was almost spiritual for me."

And Kravis? He wants to create jobs in New York City and support African-American businesses. He opened the New York Fund in September, 1995, and since has collared 62 New York-based companies, including A

VOLUNTEERS:

Kravis, left, confers with David Rockefeller

Bankers Trust, Pfizer, to kick in a million apiece. He also has enlisted a pantheon of business titans, among

them Jerry I. Speyer, CEO of Tishman Speyer Properties; Richard D. Parsons, president of Time Warner; and Walter V. Shipley, CEO of Chase Manhattan. They focus on their own backyard. They and their high-powered staffs "have said to me, 'I'd like to give back to the city, but I didn't know how,'" says Kravis. "We need a vehicle where people are learning something and doing some good."

PAYBACK TIME. "Do-gooder" is not Kravis' accustomed public role. He was pilloried through the 1980s for buying out companies, including RJR Nabisco, in 1988, then piling on debt and laying off thousands—all for huge fees. Kravis' co-heads KKR, which, having raised a \$1-billion fund in 1996, is the world's largest leveraged buyout firm.

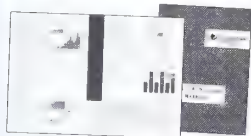
Yet Corporate America has long embraced similar strategies as important to enhancing shareholder value. And Kravis' lofty perch—replete with money, access, and power—now affords him a unique opportunity to make

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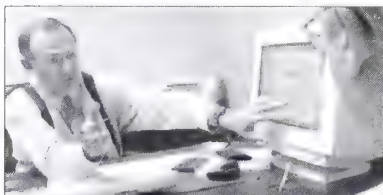
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the resources of New York's fractious business world. Financial services is the biggest industry in New York, and as the biggest financial-services client in town, KKR has paid billions in fees over the years to New York banks and brokers. Kravis is, in effect, calling in chits—and few of New York's money-men want to turn him down. "There is a very, very strong personality and driven person behind [the fund]," says David H. Komansky, CEO of Merrill Lynch & Co. and a fund board member. "Henry is not in this to fail, and neither are we."

MISSED GOAL. Over the years, Kravis has raised millions for charities. But it was financier David Rockefeller, whose New York City Partnership brought business leaders together in 1979 to address housing and education, who inspired him. Kravis says a few years ago Rockefeller gave him this advice: "The main thing is to be personally involved in giving. Set up something creative, innovative—and be personally involved." And at age 54, Kravis may have an eye on the history books. "He would like to be remembered for more than RJR," says Deryck Maughan, co-CEO of Salomon Smith Barney and a fund board member.

If the fund succeeds, it could do more than burnish Kravis' image. It could provide a blueprint for other cities' elites to support business development. It will be an uphill battle, though. While some U.S. business communities, such as Cleveland, have mobilized successfully to back real estate projects, Detroit's Renaissance Center in the 1970s and Peter Ueberroth's campaign to rebuild riot-scarred Los Angeles in the 1980s both were embarrassing flops, doomed by incoherent business plans.

The New York City fund has encountered early problems of its own. Even Kravis, a consummate fund-raiser, remains short of his \$100 million goal. Moreover, his staff has found it difficult to find projects that meet the fund's criteria: create jobs, earn decent returns, and nurture important industries and African-American-owned businesses. Of about 250 proposals, in fact, the fund has invested only in seven, committing just \$12 million. And the projects actu-

ally under way aren't close enough to fruition to assess their success.

But Kravis' venture has several promising attributes. It is modeled after KKR, wherein Kravis and his 10 partners evaluate potential investments, then watch over them until they can be sold for a handsome return. Indeed, the fund is a for-profit operation that pledges to return its investors' principal in 15

as a perk, network with others in the fields. "It mixes business and pro bono stuff," says Mahmoud Mamdani, a managing director at Morgan Stanley, Dean Witter, Discover & Co. who advises Sylvia's.

The networking can blossom in unexpected ways. At an October meeting of the fund's media group, Jack Gergen, a senior vice-president at CBS Inc., noted that all three networks are headquartered in New York and all will spend hundreds of millions to switch to digital technology in the next few years. Why not use their clout with vendors and stations to ensure that some of the equipment be manufactured in New York? Claire Shulman, Queens borough president, responded: "I have land lots in Queens for new factories. Gergen is meeting with other network executives to pursue the notion.

In another deal, Kravis pressed Komansky to recruit Merrill Lynch clients as tenants for Brooklyn retail strip. So far, Rite Aid, State Farm,



At its heart, the fund represents a convergence of New York's best financial and business brains, all working for free

UPTOWN EATS: CHAZEN WITH SYLVIA AND VAN WOODS AND THEIR WARES

years, albeit without interest. Says Kravis: "We take this as seriously as KKR deals. Only we are looking for returns in job creation as opposed to huge rates of return." Like KKR, too, the fund diversifies its bets—across retailing, health care, media, and other industries at the local economy's core. "They imagine a city to be like a good balanced stock portfolio," says Bennett Harrison, professor of urban political economics at the New School for Social Research. "If some of the bets don't pay off, the portfolio still does well."

The fund's biggest strength, though, is the volunteer legion of business brains that augments its small, paid staff. Below the board level, top-flight bankers and executives serve on six sector groups, from manufacturing to education. Members generate projects and,

and Citicorp have signed on. And Al Waxman, came up with the idea of backing a managed care group for Medicaid recipients in Queens and Brooklyn with a \$2 million investment. It has already added more than 100 jobs.

Kravis spends a good chunk of his time overseeing the fund's work and twisting new arms. His involvement establishes that no matter how busy he is, no matter how important you think this is something worth doing," says Kathryn S. Wylde, whom Kravis plucked from the NYC Housing Partnership to run the fund. Will it work? Kravis surely won't change New York overnight—but he may create some jobs, bankroll a few companies, and Sylvia's collard greens go national.

By Leah Nathans Spiro in New York



NET NIGHTMARE FOR THE MUSIC BIZ

Despite piracy woes, Web distribution seems unstoppable

Last September, Capitol Records caused a stir when it offered for download a new single by Duran Duran over the Internet for 99¢. Before then, the label had sold music digitally over the Web. It quickly turned into a nightmare: Record retailers were outraged, credit-card companies were wary, and questions about copyright and antipiracy measures proved murky as ever. So this April, when Capitol releases a new album by one of its biggest stars, Bonnie Raitt, sales will come the old-fashioned way—through local record stores. “We’re taking a conservative approach,” says Liz Heller, Capitol’s executive vice-president of Capitol Records Inc. “We’re taking a conservative approach.” As soon as a CD is released, most new songs will be on underground,

unauthorized Web sites known as MP3 sites (named after an audio-compression scheme). Hundreds of these sites—some illegally offering copyrighted material, others legally presenting uncopyrighted music, with advertising from big companies such as Intel Inc.—offer thousands of songs for free. They can be downloaded in minutes, stored on hard disks, and transferred to recordable CDs. They’re the rage on college campuses, where students spend hours making compilations to swap with friends.

MP3 sites have yet to make a notice-

able dent in CD sales. But their growing popularity, fueled by the spread of high-bandwidth Internet connections and recordable-CD players as cheap as \$200, is causing alarm in the music industry. Electronic distribution of music is coming fast, and it will alter industry fundamentals that have changed little since the days of 78s. Just last week, PolyGram CEO Alain M. Lévy announced he is forming a board-level committee to examine the impact of the Net.

POWER SHIFT. What’s certain is that artists will gain power, while record companies’ huge assets and power bases in manufacturing and distribution, as well as relationships with retailers, will become less important. “The balance of power will change,” said Thomas Dolby Robertson, a musician and chief executive of Headspace Inc., a San Mateo (Calif.) venture that develops technology to deliver music over the Internet.

Fearful as they are of the threats, major labels acknowledge the opportunities and are taking tentative steps into the digital realm. Sony Music, Warner Music, and PolyGram have begun to put up sites that take orders online and send customers CDs through the mail. Most also offer audio samples—but only in “streaming” formats that can’t be stored. New York-based Jupiter Communications Co. estimates that the online retail business will grow to \$1.7 billion by 2002, or 7.5% of the overall music market, up from \$50 million in 1997.

But with security still lacking—and fearful of straining their ties to retailers—the six majors (Bertelsmann, EMI-Capitol, Universal, PolyGram, Sony Music, and Warner Music) are sticking to promotional use, stopping well short of commercial downloads. But by doing this, they risk missing the boat, just as film studios did in the early 1980s when they opposed the VCR, only to cede lucrative distribution and retail markets to Blockbuster Entertainment and others. “The major record labels have taken their heads out of the sand but still have their feet in concrete,” said Tom McPartland, president and CEO of TCI Music Inc., an affiliate of cable giant Tele-Communications Inc. that delivers music digitally via satellite, cable, or the Internet.

Instead, smaller, more entrepreneurial companies are setting the pace. Liquid Audio Inc. in Redwood, Calif., and AT&T unit A2B are promoting new software systems that compress, encrypt, and

DIGITAL DILEMMA

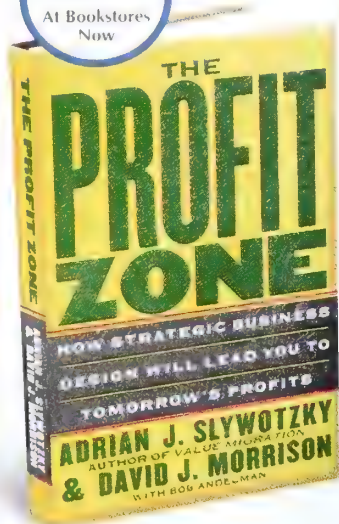
Record companies are struggling with the prospect of delivering music CDs over the Internet

PROS	CONS
• Lower costs • Free global distribution • One-to-one marketing	• Prospect of rampant piracy • Backlash from bypassed record stores • Problems with cyberpayments

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Entertainment

track music delivered over the Net. N2K Inc., which runs the popular MusicBk retail Web site, cooperated with David Bowie in 1996 to deliver more than 300,000 free downloads of a single. Last July, it went commercial and has since electronically distributed more than 4,000 99¢ singles by artists affiliated with independent labels. "It's still no proof of concept than anything else," says N2K CEO Larry Rosen. "But the idea definitely makes sense."

BIGGER SELECTION. If their concern about piracy and control can be solved, record companies could win big with digital delivery. In addition to lower costs, they'll be able to target individual fans to promote albums, concerts, merchandise. And while most of the thousands of CDs in print are not available in most stores, the Internet will enable labels to sell entire catalogs to anyone, anytime, anywhere. There will be new marketing tools, too: Already some CDs direct consumers to Web sites that unlock additional music on the digital Net provide great opportunities, as we love that," said Cary Sherman, senior executive vice-president for the Recording Industry Assn. (RIAA).

Still, policing this market will be difficult. The RIAA has only three full-time staffers searching for illegal MP3 sites. They send out five or six cease-and-desist letters daily. In January, the RIAA settled three separate federal lawsuits against MP3 operators, waiving millions of dollars in damages as long as the defendants stop pirating music. But with more than 30,000 music Web sites, Sherman concedes that "it's extremely difficult to enforce." That's why the industry prefers technological solutions, using better tools to ferret out Web pirates and enlisting the cooperation of Internet service providers and hardware makers in preventing illegal distribution.

Long term, such devices are certain to emerge. Meanwhile, record companies face a difficult transition. They remain kings of content but will have to begin embracing the new paradigm as it undermines current sources of power and profit. And in the online realm, labels have little value as brands. Aside from a few genre-specific labels such as Blue Note, Motown, and Deutsche Grammophon, consumers don't associate artists with their record companies. So label-independent sites such as N2K and CDnow are better positioned to offer a wide selection. To stay ahead, the big record companies will have to move to a new beat.

By Steven V. Brull in Los Angeles



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PERSONAL WEALTH



No one can accuse Genzyme Corp., the biotech giant based in Cambridge, Mass., of being a technological laggard. Its scientists work at the forefront of biological research, while computer-controlled production equipment churns out hundreds of different advanced compounds.

So imagine the reaction of Robert Cowie, Genzyme's chief information officer, when he realized in 1996 that every major system at Genzyme would be unable to run with dates in the next century—the so-called Year 2000, or Y2K, computer bug. If left unfixed, the production equipment, research and development computers used to analyze data, and the computers handling ordering and billing would all stop working on or before Jan. 1, 2000. Thanks to an early start, Cowie expects to have all his systems repaired well ahead of the deadline. "Our businesses won't be so fortunate, he believes. 'People will expect to be complete by the end of this year, or it will be too late,'" says Cowie. "But there are still many companies that haven't done anything yet."

Cowie is right about the overall lack of preparedness for the Year 2000—and there's mounting evidence that a lot of businesses are in for a nasty shock. Up to now, skeptics have been able to pooch-pooch the Year 2000 as a relatively easy-to-fix bug, a simple example of overhyped hype by consultants looking for a buck. But there's a growing alarm in Washington and elsewhere. The Securities and Exchange Commission has recently been strongly urging companies to start reporting the effect of Year 2000 on their earnings. "Many people think it's totally exaggerated," says Percy Barnevik, chairman of Swiss-

Swiss industrial giant ABB Asea Brown Boveri Ltd., one of the world's largest companies. "But it is a really big challenge."

ES OF PROGRAMMERS. Indeed, the Y2K bug is shaping up to have a profoundly negative impact on the U.S. economy—starting almost immediately. According to a new analysis prepared for BUSINESS WEEK by Standard & Poor's, the growth rate in 1999 will be 0.3 percentage points less as companies divert resources to fix the problem. The Y2K bug could cut half a percentage point off growth in 2000 and early 2001. That would be the same size as the ex-

pected economic damage from the turmoil in East Asia.

All told, the Year 2000 bug could cost the U.S. about \$119 billion in lost economic output between now and 2001. "The Year 2000 bug will certainly hurt the economy," says DRI chief economist David A. Wyss, "and it could be a real killer if more of the problems are not fixed."

It's not only the growth rate that will be affected. Starting in 1999, inflation will be higher than it otherwise would have been and productivity growth will be lower. The reason:

Instead of creating or installing new productivity-enhancing programs, every company that uses computers is diverting money and skilled workers into patching old programs.

Think of it as a town threatened by a rising river. Every able-bodied person—no matter what their job—is put to work stacking sandbags, while economic activity in the rest of the town slows down. In the case of the Y2K bug, experienced programmers and computer-science PhDs are doing what is essentially unproductive labor.

And the amount of skilled labor needed is enormous. Finding, fixing, and testing all Y2K-affected software would require over 700,000 person-years, calculates Capers Jones, head of Software Productivity Research, a firm that tracks programmer productivity. "People are spending huge sums of money fixing problems that are 35 or 40 years old, just to stay in business," says John Bace, research director at Gartner Group Inc.

Indeed, the demand for Year 2000 fixes helps explain why management consulting and accounting

firms have added a stunning 200,000 new workers over the past two years. Moreover, with programmers' wages soaring because of the overpowering need to fix the problem, Year 2000 has the potential to push up inflation.

Then, at the beginning of 2000, the economy is almost certain to be hit by some computer failures, since it's becoming clear that many companies have gotten a late start attacking their Y2K problems. The BUSINESS WEEK/DRI estimate assumes that 85% of software programs will be fixed or replaced, which may be optimistic: A December, 1997, survey

ZAP!

HOW THE YEAR 2000 BUG WILL HURT THE ECONOMY

Growth could take a half-point hit in 2000 as inflation rises

Cover Story

by Howard Rubin, a computer-science professor at Hunter College in New York, indicated that two out of three large companies did not yet have detailed plans in place to address Year 2000. Small companies and government agencies are even further behind.

Year 2000 is going to pose a serious policy dilemma for the Federal Reserve, which has been trying to steer a tricky course. Over the next couple of years, Fed Chairman Alan Greenspan is going to be under increasing pressure to raise interest rates as labor shortages for information-technology workers send wages skyrocketing. The problem: A rate hike in 1999 would run the risk of worsening the post-2000 slowdown.

Some analysts even worry that Y2K could send the economy into a recession. Edward E. Yardeni, chief economist at investment bank Deutsche

YEAR 2000: THE ECONOMIC DAMAGE

TOTAL LOSS OF OUTPUT
1998-2001

\$119 BILLION

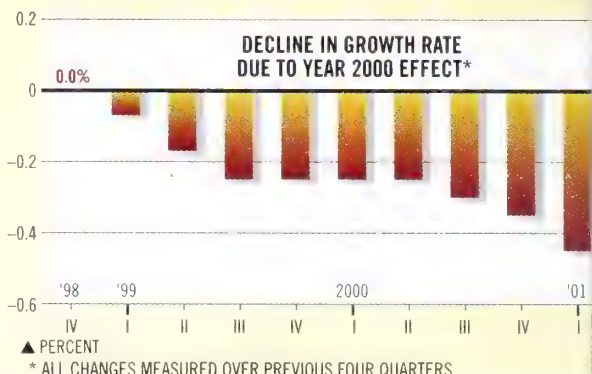
(IN 1998 DOLLARS)

Cover Story

Morgan Grenfell Inc., sees a 40% chance of a sharp downturn. One way that could happen is if there's a major failure in the government's computer systems. Each week, the federal government sends out \$32 billion in Social Security and payroll checks and payments for such mundane items as rent. Even a short delay could be a major shock to the economy.

Unfortunately, when the Office of Management & Budget issues the next official report on the government's Y2K readi-

GROWTH WILL SLOW SHARPLY...



flow of Medicare and Medicaid funds. In the worst case, tax system and the Medicare payment system will experience severe disruptions in 2000, halting the delivery of ref and reimbursement checks. "What is going to happen is government is going to say, 'It's O.K., trust us,'" says Richard M. Kovacevich, CEO of Minneapolis-based Norv Corp. "It could get scary."

NOT LOSING SLEEP. To be sure, there are some, especially Silicon Valley, who aren't concerned. "Frankly, I don't lose sleep on worrying about being Year 2000-ready," says Benhamou, CEO of 3Com Corp., the large network-equipment maker. Adds Tony Hampel, group manager for Year 2 Marketing at Sun Microsystems Inc.: "Year 2000 is an

ELECTRIC POWER

Many electric utilities realized last year that their generating plants were susceptible to Y2K problems. Severe power outages are likely, and some nuclear power plants may be shut down temporarily



ness on Mar. 15, the news is not likely to be good. On Feb. 6, the Defense Dept.'s Inspector General issued a report saying that the military has no assurance that it is purchasing Year 2000-compliant products, "which may seriously hamper the ability of DOD to perform its administrative and warfighting mission requirements." The Internal Revenue Service is struggling to meet the deadline, as is the Health Care Financing Administration (HCFA), which handles the enormous

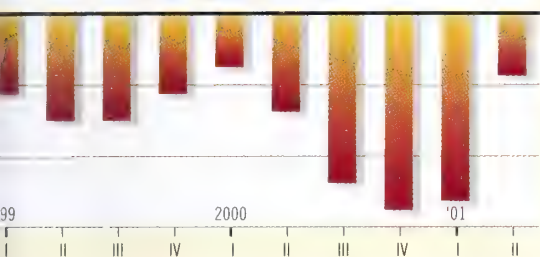
serve. "The failure to get it right will affect the integrity of the payment system, financial markets, and the performance of the domestic and the global economies," said William Donough, president of the Federal Reserve Bank of New York, in a recent speech.

How can a single computer bug turn out to be so potentially hazardous to the economy? In theory, any single instance of the 2000 bug is relatively easy to repair. But

RECESSION? The chances that the Year 2000 bug will spark

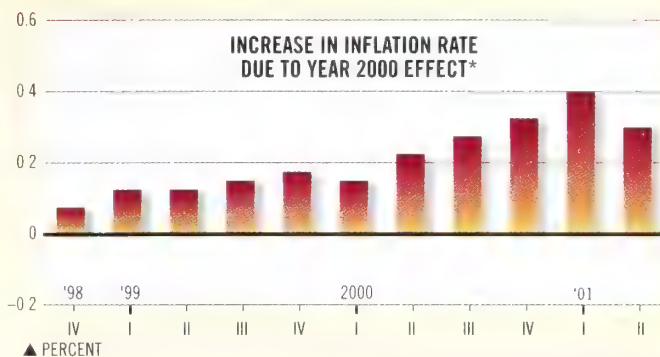
...PRODUCTIVITY WILL SUFFER...

DECLINE IN PRODUCTIVITY GROWTH RATE
DUE TO YEAR 2000 EFFECT*



...AND INFLATION WILL RISE

INCREASE IN INFLATION RATE
DUE TO YEAR 2000 EFFECT*



DATA: BUSINESS WEEK, STANDARD & POOR'S DRI

number and complexity of computer programs that makes turn the process of fixing the programs—also known as “remediation”—into a herculean task. Consider a household analogy. If you have to change one lightbulb or one electric switch in your house, there’s no problem. But if you have to replace the lightbulbs and electric switches in everything you own, including your refrigerator, your car dashboard, and your furnace, it becomes a

that programmable controllers—which have replaced mechanical relays in virtually all electricity-generating plants and control rooms—may behave badly or even freeze up when 2000 arrives. Many utilities are just getting a handle on the problem. “It’s probably six months too soon for anyone to try to guess the complete extent of the problem,” says Charlie Siebenthal, manager of the Year 2000 program at the Electric Power Research Institute, the industry group that serves as

GOVERNMENT

For problems exist in the Internal Revenue Service and by other agencies. State and local governments are way behind fixing date-sensitive programs used for tax collection, payrolls, and other payments.

time-consuming and expensive process. Indeed, what makes the Year 2000 particularly troubling is that it affects stand-alone computers and the embedded processors built into all kinds of modern equipment, from automated machinery to power plants to cars to cellular telephones. Last fall, Phillips Petroleum Co. engineers ran Year 2000 tests on an oil-and-gas production platform in the North Sea. The result: In a simulation, an essential safety system for detecting harmful gases such as hydrogen sulfide got confused and shut down. In real life, that would have rendered the platform unusable. Similar problems can occur in almost any kind of modern manufacturing that involves sensors and control machinery. “There will be facilities where they go on and turn on the machines and they won’t go on,” says Dean Mann, head of the technology division at engineering firm Harsco & Veatch, the world’s largest provider of power plants. In particular, electric utilities are only now becoming aware



an information clearinghouse. “We don’t know” if electricity flow will be affected, he said.

Nuclear power plants, of course, pose an especially worrisome problem. While their basic safety systems should continue to work, other important systems could malfunction because of the 2000 bug. In one Year 2000 test, notes Jared S. Wermiel, who is leading the millennium bug effort at the Nuclear Regulatory Commission, the security computer at a nuclear power plant failed by opening vital areas that are normally locked. For that reason, the NRC is in the process of issuing a letter requesting confirmation from utilities that their plants will operate safely come Jan. 1, 2000. Given the complexity and the need to test, “it wouldn’t surprise me if cer-

sharp downturn are pegged at 40% by economist Yardeni

Think of a date—say, Feb. 10, 1998. In the U.S., no one would object if you wrote that date as 2/10/98. People would know what you meant.

So there were no worries in the 1970s and '80s when programmers wrote software that represented years with only the last two digits rather than all four—"85" rather than "1985."

Programmers thought they were clever since they were conserving memory, which was expensive back then. Despite falling memory prices, the practice continued into the 1990s—out of habit and inertia.

Unfortunately, these programs interpret the year 2000 as 1900, which has the same last two digits. So any program with a date—billing, payroll, inventory, bank accounts—could crash or give misleading answers on Jan. 1, 2000, or before, since software that does scheduling or planning often uses dates a year or more in the future.

For example, if a program figures the age of a person

HOW DID WE GET INTO THIS MESS, ANYWAY?

by subtracting the date of birth from the current year, then starting in 2000 it will look as if everyone less than 100 years old will have a negative age. Some other daunting errors: a missing paycheck, a scrambled bank statement, the shutdown of a factory, or a power plant's inability to deliver electricity. Or the software can simply freeze up. "We

feel you'll be a lot luckier if the system stops functioning," says Larry Olson, chief information officer for the state of Pennsylvania. "It might be two months before you realize you're getting bad information."

The Year 2000 bug also shows up in microprocessors built into machinery, from automated assembly lines to cellular telephones. "Our biggest concern is that we miss an integrated circuit buried down inside somewhere that would have a cascade effect," says Bruce Colgate, process control manager at Phillips Petroleum Co. This is one bug whose effects may only be known when it bites.

tain plants find that they are not Year 2000-ready and have to shut down," says Wermeil.

By contrast, the securities industry, big banks, and the Federal Reserve have been taking Year 2000 seriously for years. Chase Manhattan Corp. is spending \$250 million on the problem, while Wells Fargo & Co. will ultimately deploy 400 people to fix y2k. Later this year and next year, Wall Street firms will run an industrywide test simulating the rollover to Jan. 1, 2000.

But smaller banks are lagging way behind. According to an extensive new survey from accounting firm Grant Thornton, community banks are only spending an average of \$7,000 each on the bug. "They are not taking it seriously enough," says Diane Casey, national director of Thornton's financial-services practice. Only 44% have tested their vaults and other time-sensitive security systems for Year 2000, raising the possibility that they will either be locked out or that doors and vaults will spring open on New Year's Day, 2000.

PREOCCUPIED IN ASIA. These smaller banks, which typically outsource check processing and other computer-dependent operations to outside service providers, are assuming that those companies will handle the problem. But bank-service providers themselves are faced with the tough prospect of fixing their own systems. If outside vendors don't get the problem corrected, "banks are then in a real bind," says Mark L. O'Dell, director of the bank-tech-

BANKING AND FINANCIAL SERVICES

Most large banks, the Federal Reserve, and the exchanges should be well prepared. But foreign banks and small U.S. banks are lagging. The result: Disruptions in the financial system

Cover Story

nology division at the Office of the Comptroller of the Currency. Another danger to the U.S. financial system comes from abroad. European and Asian banks are far behind their U.S. counterparts. In Europe, banks are focusing on the enormous task of converting their financial programs to handle the euro, rather than fixing y2k. "Western Europe will not achieve Year 2000 compliance for even 65% of the applications that need Year 2000 repair," says software expert Jones.

And the situation in Asia may be even worse, since banks in those countries are more preoccupied with surviving the

current economic threat than worrying about Year 2000. "Y2K could trigger a whole new round of country debt negotiations," warned Philip Kozloff, a member of Citibank's Credit Policy Committee, speaking at a Securities Industry Association conference in January. Adds Yardeni: "If foreign banks fail to comply, that could have a serious impact on world trade."

Closer to home, state and local governments are lagging even further behind the federal government. In Massachusetts, for example, according to a report released on Feb. 1, more than 40% of state agencies had not yet even begun



GETTING LATE It takes time to test Year 2000 fixes. Large companies just starting their Y2K repairs are in big trouble

to become Year 2000-compliant. "It is likely that certain systems will not attain Year 2000 compliance in time and that alternative processing methods will be needed," wrote State Representative A. Joseph DeNucci, whose office prepared the report. Massachusetts isn't alone. Only about one-third of states are in good shape, estimates Larry Olson, chief information officer of Pennsylvania, which got an early start on fixing Year 2000 problems. "Everybody else will have significant problems." What's more, the problems reach down to local level, including school systems, which must run payroll systems, student records, and operate other date-sensitive systems. The fixes could be quite expensive: The Columbus Public School system, with 65,000 students, may have to pay \$1 million to fix its most significant applications.

SILVER-BULLET SOLUTION. Is there any chance of avoiding a major economic upheaval from Y2K? Yes, but it will take a great effort. Smaller companies and organizations still have a chance to fix their typically less complicated computers and systems. And utilities and manufacturers with embedded systems problems can fix them—if they start right now. "It's not too late, but they can study for a year," says Kothmann.

For a large company or organization that has not yet started dealing with Year 2000 is in big trouble. While software tools do exist for identifying trouble spots and speeding

finding the trained workers they need to fix their Year 2000 woes. A just-released study from the Information Technology Association of America shows that the U.S. already has 350,000 job vacancies for computer scientists and programmers that are not getting filled. "The big issue for corporations is going to be around resources," says Cowie. "If you need to change your systems, and you have to get programmers in to do that, it will be very hard."

To be sure, far-sighted companies have up to now solved their Y2K problems by

simply installing new software and hardware. But such major productivity-enhancing projects take even longer than fixing old software. "Until now, many people have been ripping things out, installing new software," says William T. Ruckle, managing director of Ernst & Young's Year 2000 business. "It's getting too late to do that." Adds ABB's Barnevik: "Some of the biggest problems will come when people have planned to substitute new systems for old ones. If there are problems, it will be too late to rebuild the old system."

What happens next, aside from everyone working very hard to fix the problem? Some organizations that have their Year 2000 bug under control are getting ready to turn it into

Cover Story

MANUFACTURING

Most large companies are on top of the problem, but they are vulnerable to problems at smaller suppliers. Industries such as pharmaceuticals and petroleum refining depend on timing-sensitive computer programs

a competitive advantage. "Solving this problem gives us a marketing tool that we plan on using," says Pennsylvania Governor Tom Ridge.

Most managers, though, are going to have to start thinking

about contingency plans and workarounds. "There's no question that things will fail," says Judith List, who runs the Year 2000 effort for Bellcore, which develops communications software. "What Bellcore recommends is that you focus on the mission-critical systems first."

Year 2000 is a unique and unprecedented economic event. Previous jolts to the economy, like the gulf war and the oil price shocks of the 1970s, were surprises. But Year 2000 is the first economic disaster to arrive on a schedule. The great danger is that the U.S. economy will not be ready to welcome the millennium.

By Michael J. Mandel, with Peter Coy in New York, Paul C. Judge in Boston, and bureau reports



they only solve part of the problem. "There is no silver-bullet solution," says Jean-Charles André, director of Year 2000 services for IBM Global Services.

In particular, no software tool can eliminate the need for testing Year 2000 fixes once they are made—and testing a dedicated software program is so time-consuming that it is likely to be one of the biggest barriers to finishing on time. For a large company that has not started making fixes, the great difficulty is completing tests before the deadline, according to Jones. The same is true for governments: "If you're not well on your way now, you just don't have time to do anything," says Olson.

Small companies and other organizations may also have trouble

COMMENTARY

By Aaron Bernstein

WHY WORKERS STILL HOLD A WEAK HAND

The new labor pact between Caterpillar Inc. and the United Auto Workers (UAW) reached on Feb. 13 is a case study of the conflicting trends in today's economy. On the one hand, Cat has posted record profits for four straight years. On the other, the recent labor deal calls for newly hired workers to be paid 70% of the \$20 an hour that current workers earn. It also provides minimal raises for current union members (table).

The UAW had little choice but to go along with such onerous terms—similar to those won by Caterpillar rival Deere & Co. last October. The alternative was to see more jobs at both companies lost to outsourcing. Throughout the 1990s, both companies have cut costs by farming out work to suppliers and by expanding in lower wage, nonunion plants in the South and overseas.

SCOURING FOR SKILL. Indeed, the union's concessions underscore the degree to which employers still have the upper hand, despite jobless levels that are the lowest in a generation. Though most companies today are scouring for skilled workers, many also continue to control costs by outsourcing, downsizing, and off-shore production; stiff global competition all but rules out price hikes. So although average wages finally outpaced inflation by 2% last year, they still remain 3% below their mid-1980s peak—and even fall below 1973 levels, according to the Bureau of Labor Statistics. These trends hold true for union and nonunion workers alike. "Wages are rising, but they haven't taken off," says Nicholas S. Perna, chief economist at Fleet Financial Group. "Employers have learned how to manage their labor costs."

The UAW's stinging defeats at Cat and Deere show how little bargain-



CLAWLESS IN PEORIA: Cat threatened the UAW with outsourcing

ing power the union has. It first struck Cat in late 1991, when the economy was barely out of recession and unemployment ran at nearly 7%. Cat refused to sign a contract modeled on the union's contract with Deere. Such pattern-bargaining, Cat argued, had been rendered obsolete by globalization. Its largest rival, the company said, was no longer Deere but Japan's Komatsu Ltd., where wages were below those at Cat and Deere.

Cat won the battle by threatening to replace strikers. In mid-1994, the union suffered an even bigger setback in a second walkout. This time, Cat made good on its threat by bringing in low-wage replacement workers from one of its Southern plants. Several thousand of the union's 12,000 members panicked and crossed the picket lines. The strike was officially ended in December, 1995.

In retrospect, Komatsu wasn't the threat it promised to be. In part, it was hurt by a strong yen and poor management. In addition, Cat Chief Executive Donald V.

Fites did a masterful job of making his company globally competitive by cutting costs and initiating a sizable restructuring. Result: Cat's sales jumped 15% last year, to \$18.9 billion, while profits soared by 22%, to \$1.67 billion.

DEERE SEASON. Deere, too, has prospered and is getting an added boost from the same two-tier wage structure Cat is now adopting. Deere has racked up record profits for 18 of the past 19

quarters. It has added 220 UAW workers since the new pact was signed last fall, all at wages about half those of Deere's current 9,500 union members. And it faces little problem finding recruits, despite Iowa's low jobless rate of less than 3%. Last summer, the company got 9,000 applications for 200 slots, even though it warned applicants that the jobs were only temporary and would pay \$10.40 an hour, nearly a third less than union wages.

Companies like Deere and Cat hold particularly strong hands in today's economy. Their unionized workers are highly paid by blue-collar standards, and legions of workers stuck in lower-rung jobs are eager to take their places. Plenty of nonunion companies, too, use downsizing and cost-cutting to ho wage hikes at bay. Across the economy, the upward pressure on wages that typically comes from low unemployment is being held in check by the crosswinds of the global economy.

THE UAW FOLDS

Highlights of Cat's new labor pact:

CURRENT WORKERS

One pay raise of 2% to 4%, plus bonuses of 3% in three of the six years

NEW HIRES Start at 70% of current employees' \$20 an hour

CONTRACT LENGTH

Six years, double the old pact

DATA BUSINESS WEEK

Bernstein covers labor for BUSINESS WEEK

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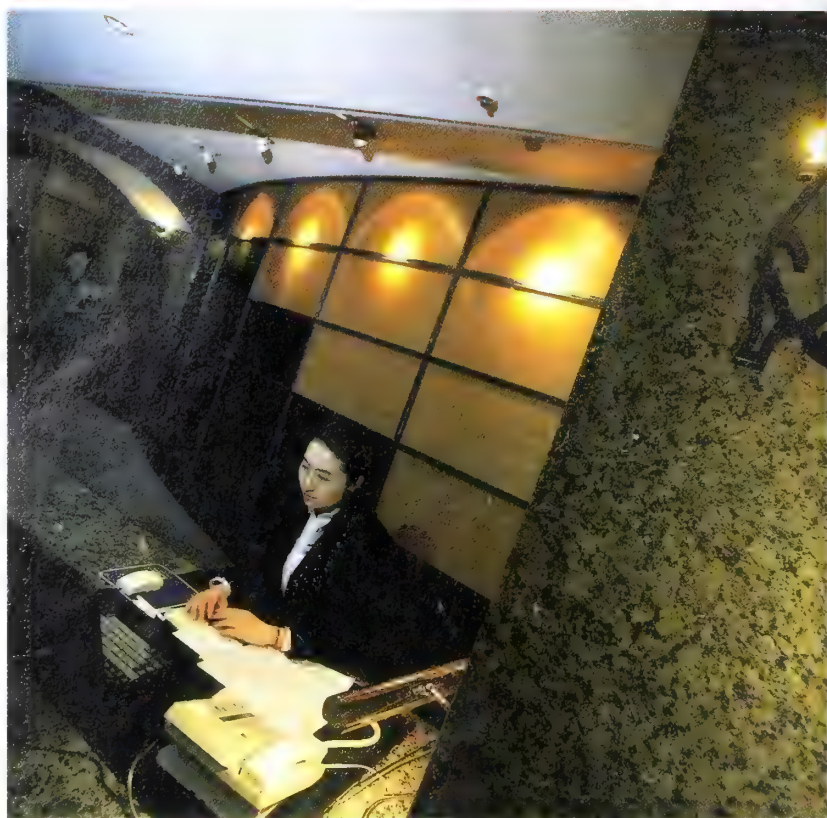
BULLISH ON JAPAN

For Merrill and others, bank scandals have opened doors

Back in 1978, Merrill Lynch & Co. had big dreams of selling stocks, mutual funds, and financial advisory services to rich Japanese investors. But it underestimated how hard it would be to lure the Japanese away from local brokers despite their unscrupulous practices, sky-high fees, and dismal returns. Merrill also misjudged the willingness of the Ministry of Finance to allow foreigners into Japan's markets. Defeated, Merrill closed its six retail branches in 1993. But now it's back, betting that the failures and scandals shaking Japan's financial-services industry will finally give it an opening. Its aim, says Merrill Lynch Japan Inc. Chairman Hisashi Moriya, is to be "Japan's most trusted financial adviser."

To reach that goal, Merrill is spending up to \$300 million to take over 30 branch offices and 2,000 brokers from shuttered Yamaichi Securities Co., until last November Japan's fourth-largest investment bank. By late summer, Merrill will offer domestic and global investment trusts—as mutual funds are known in Japan—plus convertible bonds and foreign currency investments.

GOOD BUZZ. Merrill is also counting on its reputation as one of Japan's top players in corporate bond underwriting and equity trading to help it expand its retail arm. "Scandals anywhere in the world are an opportunity," says Merrill Lynch International



OPEN FOR BUSINESS The lure is a piece of Japan's \$10 trillion in private savings

Chairman Winthrop H. Smith Jr. They're an opportunity for more than Merrill. Fidelity Investments, GE Capital Services, and Citibank all want to grab a bigger piece of Japan's \$10 trillion in private savings. With only

Knocking at Tokyo's Door

MERRILL LYNCH

Plans to spend \$300 million to open a nationwide brokerage. It will sell mutual funds, convertible bonds, and foreign currency products to Japanese investors.

FIDELITY

Raised \$2.5 billion for six mutual funds and is likely to sell funds through domestic bank branches. It is also launching a major direct marketing effort, including a Japanese-language Web site.

CITIBANK

Already an established retail name in Japan, Citibank will link its branches with the nation's postal savings network. It also will offer a dual-currency credit card.

GE CAPITAL

Just announced a \$1.2 billion joint venture with Toho Mutual Life Insurance to sell life and health coverage.

DATA: BUSINESSWEEK

6% of Japanese people invested in securities, much of that money is languishing in bank or Postal Savings System accounts, where it earns less than 1%. But more than scandals are giving foreigners hope. For decades, they've been effectively shut out of Japan by exclusive ties between the MOF and Japanese banks and brokers. Now, even the Ministry realizes Japanese consumers must earn far greater returns to invest for a rapidly aging population. The big reason Prime Minister Ryutaro Hashimoto is pushing his "Big Bang" plan to promote more financial industry competition by 2001. While the plan is daunting to many cossetted players, "the truth is, investors in Japan will be big beneficiaries," says U.S. Commerce Secretary William Daley.

The early buzz on U.S. competition is promising. Fidelity, which started selling investment trusts directly to the Japanese in 1995, now offers them six mutual funds. With \$2.5 billion under management, Fidelity's assets are growing at a 50% annual rate. Last month, Fidelity set up pilot offices with Sanwa Bank, Sumitomo Bank, and Long-Term Credit Bank of Japan to familiarize Japanese bankers with its products. Fidelity hopes eventually to market its funds via lenders' branch networks. Fidelity has also launched a Japanese-language

page (www.fidelity.co.jp) that will financial-planning tools, market, and fund-performance data. Goldman Sachs & Co. is also selling funds through Nikko Securities Co. and Koku-securities Co.

Citibank, meanwhile, is redoubling efforts to woo the Japanese. Its automated teller machines now operate 24 hours a day, in contrast to Japanese banks' terminals, which shut down at night. Citi expects to win Diet approval for its 65 ATMs to the 20,000 terminals at post offices throughout Japan. In addition, Citibank is offering customers something besides convenience—safety. As worries over the stability of Japanese lenders have mounted since the failure of Hokkaido Tokai Bank Ltd. in November, customers have been lining up at Citi's branches to open accounts. In April, Citi will roll out a new credit card that will let holders take advantage of the yen in the value of the yen by paying their balances in dollars, if they choose. Insurers are also in for foreign competition. GE Capital Services, General Electric Co.'s financial services unit, has set up a \$1.2 billion joint venture with Toho Mutual Life Insurance, a bankrupt-plagued insurer with a junk rating, to sell life and health coverage. The venture will be up against American International Group, which recently hired 800 former Yamaichi employees to boost sales.

LINE U.S. financial-services firms may have reason to be optimistic. But they still face a tough slog. Merrill's Smith won't expect his new retail unit to turn a profit for three years. And teaching American-style practices to Japanese won't be easy. Japanese brokers, for example, are judged by their commission volumes, not by how well they serve clients' money. As a result, Takumano, a financial consultant and former Yamaichi executive, wonders whether Merrill will be able to impose American-style compliance methods on bro-dealers used to "walking a very fine line between the legal and illegal" to drum up business.

Still, the time is ripe to try. The Japanese are offering ordinary Japanese choices and better returns. They also may end up teaching Japanese firms how to compete in an industry thrown open by the Big Bang. A while ago, Toyota and Honda shook the Detroit auto industry out of its complacency. Now, it looks like some American financial powerhouses are about to do the same in the favor.

By Brian Bremner in Tokyo

DEALS

SOCGEN: GROWING ONE LITTLE BANK AT A TIME

But is Cowen big enough to help the French giant in Europe?

Daniel Bouton, chief executive of France's Société Générale, has no illusions about going head-to-head with the world's investment-banking giants. Instead, he aims to carve out global niches where his \$365 billion bank can excel. "We're don't intend to compete globally [across all industries] with Merrill Lynch or Goldman Sachs," says Bouton.



The latest in a series of acquisitions, Bouton, 47, plans to spend \$615 million to purchase Cowen & Co., a small Wall Street investment bank with a strong presence in technology and health care. The object: to take Cowen's underwriting and research expertise across the Atlantic. "As excited as we are about the U.S., we're even more excited about the opportunity to work with growth companies in Europe," says Curtis R. Welling, New York-based CEO of Société Générale Securities Corp.

SIZE RULES. SocGen is not the first European bank to go shopping for smaller U.S. investment banks. Swiss Bank Corp., for example, bought Wall Street's Dillon Read & Co. But SBC then merged with Union Bank of Switzerland after concluding that in the increasingly competitive world of investment banking, size rules. Indeed, it's unclear whether the expected Cowen acquisition will give SocGen the strength Bouton seeks. To be

sure, SocGen's equity has increased from \$2.5 billion to \$10 billion in the decade since it was privatized, and it has become France's most profitable bank. But it still lags in investment-banking rankings. In 1997, SocGen sagged to 9th place in completed mergers in France, behind No. 1 Goldman Sachs & Co., according to Securities Data Co.

SocGen's lagging position in global markets has prompted Bouton to snap up financial concerns in Europe and Asia, including the private banking business of London-based Hambros PLC, the asset-management business of the former Yamaichi Securities Co. in Japan, and two minor U.S. investment banks besides Cowen. If the Cowen deal goes through, SocGen will have spent more than \$1.5 billion on acquisitions in the past 12 months. But analysts question whether this

BOUTON:

SocGen has deep pockets and will keep shopping

will be enough. "They are starting late and they don't have sufficient critical mass to

begin with," says Mark Hoge, bank analyst at Credit Suisse First Boston.

Bouton is moving on other fronts. He is building a London-based fund-management business from scratch and hopes to reach his goal of \$8.3 billion in assets by 2003. To do that, Bouton recently nabbed Nicola Horrick, formerly with Deutsche Morgan Grenfell, and John Richards from Fidelity to run the business. He plans to bid this month for Crédit Industriel & Commercial, a lender the French government is selling. He won't rule out a merger with a big French competitor, such as Banque Nationale de Paris, Crédit Lyonnais, or Paribas. That would create a French institution with an asset base roughly equal to Deutsche Bank. Bouton may have a niche strategy in global markets, but that isn't stopping him from thinking big.

By Gail Edmondson, with Sharon Reier, in Paris

COMMENTARY

By Andrew Osterland and Susan Jackson

INSURANCE SHOWDOWN: WHO'S RIGHT?

Insurance may never be the same. Prudential Insurance Co.'s Feb. 12 announcement that it would convert from policyholder ownership to a stock company will likely accelerate the trend away from the traditional mutual form—largely to gain access to capital markets. But there is a hot debate over the best way to do it. Most insurers have transformed into stock companies. But under legislation passed in 15 states and the District of Columbia, mutuals could create holding companies and could sell as much as a 49% stake in their operating businesses to public shareholders. Big mutuals back the idea while some publicly owned insurers and consumer groups object. The outcome could have an enormous impact. Andrew Osterland and Susan Jackson debate the issue.

OSTERLAND: Holding companies are stronger and more flexible

Before the holding company legislation, an insurer who wanted to demutualize had to endure a costly and time-consuming process. Equitable Co. spent upwards of \$40 million on its 1992 demutualization. Now, using state laws, mutuals can create holding companies much more quickly and inexpensively. Once established, the stock subsidiary can issue stock and buy other companies, as did Des Moines-based AmerUs Life Insurance Co. when it acquired AmVestors. "We see this as a way of preserving our mutual heritage and gaining access to the capital markets at the same time," says David Drury, CEO of Des Moines-based Principal Financial Group, the largest mutual insurer yet to seek approval for a holding-company structure.

A holding company can also be a better deal for policyholders, argues Salomon Smith Barney analyst Colin Devine. Fully demutualized companies tend to come to market at significant discounts to their book value. Since most policyholders usually sell immediately the shares they receive in return for their policyholder interests, they don't get a good price. "It can be a bad deal for policyholders," says Devine.

Devine thinks the holding company alternative gives poorly performing mutuals practice at being a profit-oriented company and allows management to pick the best time to go public. "If you use the holding company

as a step on the way to full demutualization, you're not screwing policyholders," says Devine.

True, there are potential conflict-of-interest issues. Mutual managers will be compensated with options in the new stock subsidiary. Consumer advocates say if shareholders gain, policyholders will lose. But

that's the case of any company with performance pay. "There's no more opportunity here to lie, cheat, and steal

than there was before," says Scott Galenbeck, general counsel for the Iowa Department of Insurance office.

The book is still being written on how holding companies will be regulated. But given the need of the mutuals and the ordeal of demutualization, the holding company option makes a lot of sense.

JACKSON: Holding companies hurt policyholders

Under full demutualization, a major portion of the insurer's surplus is distributed to policyholders in cash or stock. Equitable's policyholders received hundreds of millions of dollars. But under most

holding company laws, policyholders don't get any stock or cash. Indeed, to get a stake they would have to buy shares in the stock company. "It's like somebody walking up to

your driveway, selling your car, and then giving you a chance to buy it back," says Betsy McCaughey Ross, lieutenant governor of New York and a foe of the plan. "What is to prevent the quiet confiscation of billions of dollars of accumulated profits that ordinary men and women were told they own as mutual policyholders?"

A mutual holding company also creates a conflict of interest since the structure has two sets of owners and a common management. The stock company wants quarterly earnings increases to push up the stock. That means lower policyholder dividends and claims payouts. The mutual company, by contrast, wants higher dividends and payouts. In the real world, though, policyholders are quiescent and management can do what it wants. "It's management nirvana," sniffs Jason B. Adkins, founder of the Center for Insurance Research in Cambridge, Mass.

One study suggests that since the mutual holding company would no longer be in the business of selling insurance directly, it might not be subject to state regulatory oversight. And some industry players also worry that holding companies will not have to abide by the same tax code as stock companies. "We want to ensure a level playing field with all our competition," says Lon A. Smith, CEO of Hartford Life Inc. He and other stock-company execs are studying the holding company issues to see what kind of threat they pose.

Full demutualization may be expensive and time-consuming, but it's definitely the fairest way for mutual companies to enter the public equity market.



Susan Jackson covers insurance from the Connecticut bureau while Andrew Osterland writes about the industry in Chicago.

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MUNICIPAL BONDS

BOND INSURERS TAKE A WALK ON THE WILD SIDE

They are backing ever-riskier issues, and getting less for it

Imagine insuring the success of a high-tech startup company. That's in effect what MBIA Insurance Corp. did late last year when it insured a \$1.2 billion bond issue for a new Southern California toll road. In backing the bonds, MBIA lends its AAA credit rating, thus guaranteeing that the principal and interest will be paid. No matter that many toll roads never make good on all their debts. Without MBIA's stamp, the bond barely qualified as investment grade.

Fierce competition in the muni market has led bond insurers to guarantee ever-riskier issues and get paid less for it. What's more, with snail-like growth in the U.S., the major guarantors are backing foreign debt. Although overseas exposure is still small—only about 3% of a total \$690 billion in insured bonds—the insurers have high hopes for foreign markets. Industry executives say they want to boost their overseas business to as much as 15% of their portfolios by 2005. That introduces a host of political, economic, and currency risks.

A CLOSER LOOK. As a result, a financial guarantor's AAA rating doesn't have the same cachet it once did. True, equity investors like the two market leaders: Shares in MBIA and Ambac Assurance Corp. are up 80% and 122%, respectively, in the past two years. But investors who buy insured bonds put less faith in the guarantee and more effort into scrutinizing the bond issuers.

"The business is largely about market share, and now virtually everything that is insurable is insured," says Clark D. Wagner, portfolio manager of Executive Investors Insured Tax-Exempt fund. The result, Wagner says, is that the insurance companies are lowering their standards. "That makes me much more cautious."

In the past, muni bond insurers earned their keep by turning high-quality A-rated bonds into AAAs. But today,



Some companies have even guaranteed junk issues, turning them into AAA-rated bonds

they also are backing more bonds that would otherwise earn only BBB ratings—the lowest investment grade.

In some cases, the insurance companies have dipped even lower and turned junk muni bonds into AAAs. Last year, MBIA insured post-bankruptcy Orange County bonds that were below investment grade. They also put their stamp on a startup toll road in the Denver airport area. "We are very positive on the L.A. and Denver areas so we felt these issues were good credit risks," says Neil Budnick, president for public and corporate finance at MBIA.

Of course, there's a good case made for the insurers casting a wide net. They're financially sound, and haven't had to pay big claims. "There's now a broader definition of what's insurable, but I don't see any increased risk," says Roger K. Taylor, president of Financial Security Assurance Inc., an Ambac Assurance Chairman and Chief Executive. Phillip Lassiter admits that some of the bonds he insures today would not have been backed five years ago. But he says the company works with the issuers to restructure deals in ways that enhance credit quality. MBIA does the same.

In the heat of battle, insurers are undercutting each other. For instance, the premium on a BBB-rated airport bond is the same as the insurance companies charged for an A-rated airport bond four years ago. That means the companies are taking on more credit risk for less money. "Premiums have dropped over 25% in the last six years," says David Vack, senior director of municipal structured finance at Fitch IBCA. Of course, the economy and the finances of most issuers have strengthened during the period, making the insurers even less likely to face a crisis. **WHAT IF?** But the financial guarantors back long-term bonds and the domestic economic environment may not always be so robust. No doubt the overseas

markets are now very different from when the insurers first took on the business. Consider the recent turmoil in Asian markets. "The bond insurers' manageable risk this time because they had little exposure," says Dick P. Smith, managing director for bond insurance ratings at Standard & Poor's Corp. Before the crisis hit, MBIA backed a \$100 million issue for the Kingdom of Saudi Arabia while Ambac insured a \$100 million bond for the Korean Development Bank. Both issuers are current in their payments. "What would have happened if they had 15% of their portfolio allocated to Asia and we were hit with the turmoil in Asia?" asks Smith.

Certainly, financial guarantors will do whatever is necessary to maintain their AAA ratings. But will investors get as much comfort in them as they once did? Now, rather than just monitoring the issuers, muni bond investors must monitor the insurers as well.

By Toddi Gutner in New York



Build a **boat.**

Someday I plan to: Teach someone to read. Run for city council.

Look up old college friends. Catch my limit of wide-mouth bass.

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COMMODITIES

CRACKS IN THE DIAMOND TRADE

A flood of low-quality gems has shaken De Beers' iron grip

Step into a Kmart or Wal-Mart Store these days, and you can pick up a diamond bracelet for \$29.99—about the same price as a toaster. That speaks volumes about the state of the diamond business. Prices of smaller diamonds are plunging—retail prices are off as much as 20% in the past year—and demand for some types of poor-quality stones is nonexistent. Why? Blame an avalanche of cheap stones from Russia and Australia.

So far, the plunge hasn't affected the pricier fine diamonds shimmering in display cases at Tiffany & Co. or Cartier. That upscale market has held its own despite deteriorating demand in financially strapped East Asia. But for how long? Some analysts fear that the abundance of supply could overwhelm the firm hold that the cartel led by South Africa's De Beers Consolidated Mines Ltd. has held over the diamond business for decades. "There is a concern that the problems in the lower-quality market could creep up to the higher end and destabilize prices," says Hilton Ashton, a diamond analyst at SMK Securities Inc. in Johannesburg.

COUNTERATTACK. It's not as if De Beers is standing still. It continues to control the bulk of the diamond trade through its London-based marketing arm, the Central Selling Organization (CSO). And it has tried to keep a tight rein on supplies and prices by jawboning cartel members and purchasing diamonds produced outside the cartel. That has helped push prices up 50%, on average, since 1986. But despite all of De Beers' efforts, the CSO has seen its share of the global market for rough, or unpolished, diamonds erode from 80% to 70% in the past five years. Many investors think that's only the beginning of a slippery slide. Since July, the price of De Beers' Amer-



LIKE A ROCK: The high end has kept its sparkle

ican depositary receipts has plummeted 37% in dollars, to \$20.

The current problems started in the early 1990s, when the Russians, in desperate need of hard currency, began dumping low-quality "near-gem" diamonds. This violated Russia's contract with the CSO, so the CSO retaliated by dropping its price for this type of rough stone. That so angered the owners of Australia's Argyle Diamond Mines, the world's largest producer of near-gem stones, that they broke with the CSO in 1996. And that, in turn, produced the avalanche of cheap stones from Russia and Australia, and, experts say, the CSO, which decided to play hardball.

By the time the Asian financial crisis hit last

summer, the diamond market was s... With so many diamonds at the low... of the market, De Beers no lo... found it effective to try to maintain... trol of the cheaper stuff. So De B... focused on the higher end. Since... vember, the CSO has contracted su... by halving sales of rough diamon... "sightholders," the 160 cutters and... ers to whom De Beers sells st... every five weeks. Indeed, Deut... Morgan Gren-fell analyst Niall Ca...

expects CSO sales to fall by... in 1998, to \$3.91 billion.

As sales drop, the carte... amond stockpile will soar... the \$4.1 billion it held in... 1997. CSO spokesman F... D.G. Walker says De B... isn't worried about its abil... finance the growing stock... The cartel has deep pocket... many investments outside... diamond business, including... ing companies such as A... American Corp. and Mir... Moreover, with a debt-to-e... ratio of only 6%, De Be... able to leverage its increas... large stockpile, which an... Ashton estimates may r... \$5.6 billion by yearend. F... Chaplin, an analyst at T. F... & Co., says the company... even borrow up to \$5 billi... fortify its war chest.

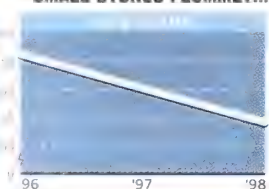
There are already signs... things are turning in De B... favor. The Russians, who...

not had a contract with De Beers... several years, have signed up again... are no longer leaking diamonds... the Asian crisis could work in the... tel's favor. "It's a dire market, so e... one is playing ball," says Mark C... editor of London-based trade mag... *Diamond International*.

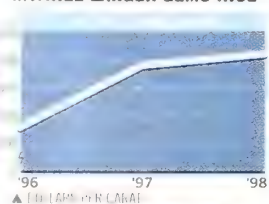
Moreover, De Beers is still cou... on its longtime marketing man... "Diamonds are forever"—to hold... The cartel believes that couples... ping for engagement and wedding... won't be swayed by cheap, mass... ket gems. "Weakness at the bot... doesn't drag down the top. Thes... two different types of consumers,"... Jeffrey H. Fischer, president of... New York-based Fischer Diamond... and the Diamond Manufacturers... porters Assn. De Beers is betting... this continues to hold true and... its costly efforts to hold the li... top-quality diamond prices will... fruit.

By Heidi Dawley in London, v... William Echikson in Brussels

THE DIAMOND MARKET SPLITS SMALL STONES PLUMMET...



...WHILE LARGER GEMS RISE



▲ DE BEERS PER CARAT
▲ FINE LAMP PER CARAT
Source: De Beers, J.A.M. Report



You wanted to save the world. Would you settle for helping a few global companies?

I've always wanted to flex your
ive muscles, make an impact,
ge the world.
agine what you could accomplish at
f the world's leading management
echnology consulting organizations.
I team with some of the most
essful companies in the world.
panies that want to explore new
ets, lead their industries,
e their futures. Working with

professionals from diverse disciplines
and backgrounds, you'd help these
companies align strategy with people,
processes and technology—a holistic
approach that transforms visionary
ideas into successful, working realities.

It's a high-energy environment
where you can leverage your skills in
collaborative, large-scale efforts. In the
process, you can learn, broaden your
perspective and shape the kind of

career you want. To explore opportunities,
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ANDERSEN CONSULTING

BY GENE G. MARCIAL

A STRONG PULSE AT MEDTRONIC

Big is beautiful, says Richard Hughes. That is, large-cap, growth-oriented companies such as Coca-Cola and General Electric are the only stocks Hughes loves—or owns. But since there aren't many such giants around, Hughes, president of Rittenhouse Financial Services, scours the world for the future Cokes and GEs. This big-stock strategy has powered Rittenhouse, acquired by Nuveen in September, to a 19.6% yearly cumulative gain since 1983. Last year, Rittenhouse's 38% gain beat the S&P 500's 33%.

So what's the next up-and-comer on Hughes's screen? Medtronic (MDT), the

world's leading maker of heart pacemakers and defibrillators. Hughes, who has been accumulating Medtronic for Rittenhouse's \$5 billion portfolio, admits it's not yet a household name. "But if you simply look at its consistent earnings growth and other fundamentals, you might think it

was Coke or GE," says Hughes.

Earnings have been growing at least 17% a year, he notes. Now trading at 55½ a share, with a price-earnings ratio of 35, Medtronic is cheap, based on its growth rate and long-term value, says Hughes. "Demographic trends favor the market that Medtronic dominates," he argues. With the baby boomers aging and more people living longer, demand for Medtronic's devices will rise. "Medtronic is at the forefront of prolonging people's lives," says Hughes.

Some two-thirds of sales come from its pacing products, chiefly bradycardia devices, which adjust slow or irregular heartbeats, and tachyarrhythmia devices, which correct rapid heartbeats. Other products include mechanical and tissue heart valves.

Analysts expect Medtronic to earn \$1.30 a share this year and \$1.56 in 1999, up from \$1.11 in 1997.

AGING BOOMERS: ROSY PROSPECTS



WHY COTT MAY BUBBLE UP

The fireworks in Dow stocks—as the market climbs to new highs—have masked the compelling values in some mid-cap plays, grouses money manager Forrest Mervine. Take Cott (COTF), the world's fourth-largest soft-drink company and the largest maker of private-label soft drinks in Britain, Canada, and the U.S. The stock has been practically lifeless, slumping from 12% in mid-October to 8% on Feb. 17—in spite of rumors that several big companies, including a major beverage maker, are eyeballing Cott for a buyout.

The death on Feb. 3 of Chairman Gerald Pencer, who controlled 29% of the company, has renewed speculation that certain groups will jockey for his block. The stock hasn't yet reflected this possibility, but it shouldn't be long before certain groups show up to bid—"if they haven't already," says Mervine, managing director of Investment Counsellors of Bryn Mawr, a unit of Pennsylvania's Bryn Mawr Trust.

Cott, with sales of more than \$1.4 billion to such customers as Wal-Mart Stores and Safeway supermarkets, is worth at least 20 in a buyout, says Mervine. He figures that sales per share are about \$20—more than three times Cott's stock price. Sales have weakened, and profit margins have narrowed as a result of the price war between Coke and Pepsi-Cola.

"Once the price-cutting ceases, earnings at Cott will explode to higher levels, partly because of new products from acquisitions it has made," he says.

Who would be interested in Cott? Mervine is betting on Britain's Cadbury Schweppes, the world's third-largest soft-drink company, which has announced its interest in acquisitions in North America to bolster its might against Coke and Pepsi. Mervine notes that the person now leading Cott is True Knowles, former president of Cadbury's Dr Pepper unit. With Pencer gone, Mervine thinks Cadbury will be emboldened to talk to Knowles

THE SODAMAKER LOOKS LIFELESS



about a deal. In October, the company hired Morgan Stanley to help the Pencer family explore options for stake. Cott didn't return calls.

HOLE IN ONE FOR CALLAWAY?

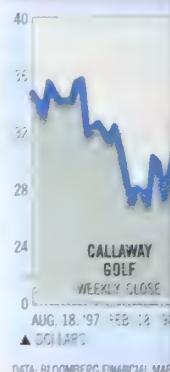
Callaway Golf (ELY) is just one of the 32 growth stocks in the \$1.5 billion portfolio of Cohen Klingenstein Marks, a New York investment firm that focuses on large companies that boast long-term earnings momentum. But, argues Managing Partner George Cohen, it's a stock with added allure. He thinks Nike may go after it.

"Nike wants to be in the sports-equipment business, and it intends to go into a full line of gear for athletes," says Cohen, who does not usually pick stocks for their takeover potential. This time, though, he thinks Callaway—apart from its strong growth qualities—looks appealing to the \$10 billion Nike for several reasons.

Callaway, the leading maker of golf gear, has the most endorsement contracts of any company from sports products, argues Cohen, and this would bolster Nike's own lineup of stars. Callaway products are "top quality and the best in the business," he adds. In golf clubs and related products, Callaway is bigger than its four closest rivals combined, notes Cohen, whose portfolio owns some \$35 million worth of Callaway shares. Equally important: The stock has been in the rough—down to 25 from its high of 38—until recently, that is, when it crept back to 31½, partly because of rumors. Callaway, which posted 1997 earnings of \$1.90 a share, is expected to make \$2.30 in 1998 and \$2.55 in 1999.

Cohen says Callaway is worth 45 times earnings. "If it's true that Nike's strategy is to buy the premium brand in sports equipment, then Callaway is the one to watch," says Cohen. Calls to Callaway weren't returned. A Nike spokeswoman says the company is developing internally the athletic-equipment unit it formed more than a year ago.

IN THE ROUGH—TILL LATELY



DATA: BLOOMBERG FINANCIAL MARKETS



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ANDERSEN CONSULTING

Corporate Scoreboard



IS THIS THE END OF THE GLORY DAYS?

Higher wages and declining profit margins lead to a slowdown in net income growth

Economists said it couldn't last. CEOs prayed it would. But in 1997 the inevitable finally happened: Corporate America's breakneck earnings growth began to falter.

Although annual sales rose 9% for the 900 companies on BUSINESS WEEK's Corporate Scoreboard—equal to the gain in

1996—net income for the year was up just 9%. That marked a significant drop from the 14% earnings growth seen in 1996. Moreover, the consensus of economists is that 1998 earnings will grow at about half this year's rate. "We've undoubtedly seen the best in earnings growth for this expansion," concludes

Allen L. Sinai, chief global economist at Primark Decision Economics.

The slowdown seemed to hit especially hard in the fourth quarter. Despite a 9% sales hike, net income registered no growth at all. Still, on an operating basis, things weren't quite as dire as they suddenly seemed. Take

The Leaders in 1997 Sales and Profits

THE TOP 25 IN SALES

		1997 SALES IN MILLIONS	PERCENT CHANGE FROM 1996	1996 RANK
1	GENERAL MOTORS	\$153,781	6%	1
2	FORD MOTOR	153,627	5	2
3	EXXON	122,089	2	3
4	WAL-MART STORES	113,428	12	4
5	GENERAL ELECTRIC	90,840	15	6
6	IBM	78,508	3	7
7	MOBIL	65,709	-19	5
8	CHRYSLER	58,622	-1	8
9	PHILIP MORRIS	56,114	3	9
10	AT&T	51,319	2	10
11	TEXACO	46,667	3	11
12	BOEING	45,800	29	33
13	DUPONT	45,079	3	12
14	HEWLETT-PACKARD	42,895	12	13
15	SEARS, ROEBUCK	41,469	8	14
16	TRAVELERS GROUP	37,609	16	36
17	PROCTER & GAMBLE	36,715	4	16
18	CHEVRON	35,009	-7	15
19	CITICORP	34,697	6	18
20	KMART	32,108	1	17
21	AMOCO	31,910	1	19
22	MERRILL LYNCH	31,731	27	27
23	CHASE MANHATTAN	30,381	11	22
24	BELL ATLANTIC	30,194	4	88
25	MOTOROLA	29,794	7	21

THE TOP 25 IN EARNINGS

		1997 PROFITS IN MILLIONS	PERCENT CHANGE FROM 1996	1996 RANK
1	EXXON	\$8,460	13%	
2	GENERAL ELECTRIC	8,203	13	
3	INTEL	6,945	35	
4	FORD MOTOR	6,920	56	
5	GENERAL MOTORS	6,698	35	
6	PHILIP MORRIS	6,310	0	
7	IBM	6,093	12	
8	MERCK	4,614	19	
9	AT&T	4,472	-20	
10	COCA-COLA	4,129	18	
11	MICROSOFT	3,895	57	
12	CHASE MANHATTAN	3,708	51	
13	PROCTER & GAMBLE	3,625	12	
14	CITICORP	3,591	-5	
15	WAL-MART STORES	3,334	15	
16	AMERICAN INTL. GROUP	3,332	15	
17	JOHNSON & JOHNSON	3,303	14	
18	MOBIL	3,272	10	
19	BELLSOUTH	3,270	14	
20	CHEVRON	3,256	25	
21	BANKAMERICA	3,210	12	
22	BRISTOL-MYERS SQUIBB	3,205	12	
23	HEWLETT-PACKARD	3,119	21	
24	ALLSTATE	3,105	50	
25	TRAVELERS GROUP	3,104	5	

DATA: STANDARD & POOR'S COMPUSTAT, A DIVISION OF THE MCGRAW HILL COMPANIES



al charges, and profits would have up about 10%, roughly half the seen in the fourth quarter of 1996. hy the disparity between strong and operating income and flat net ae? For one thing, companies—eslly those that are restructuring, or ved in mergers and acquisitions—to do more write-offs in the final er. Since 1997 saw both a record for M&A activity and a resurgence structuring, the combination ded net income. Boeing's \$1.4 bil-charge on its merger with McDon- Douglas Corp. helped drive space profits down 64% for the er, for example, while the \$2 billion e Sara Lee took to restructure its s dragged profits down a full 2% ie 900 companies. All together, the rmance of those two companies, ined with big losses at HCA/Co- a, Unisys, and Dow Jones, knocked f total profits.

SQUEEZE. Still, charges weren't nly thing dampening spirits in the quarter. An increasingly severe squeeze also depressed net profits. ibility of business to charge higher i, as measured by the government's domestic product price inflator, ened in the fourth quarter. Today, ower than it has been since 1963. le to pass along higher labor costs (112) and hamstrung by the impact e strong dollar on international Corporate America is increasingly g a hit on the bottom line. By the h quarter, profit margins, which falling all year, hit 5.5%, their low-vel since December, 1995.

spite the earnings slowdown, the my in the fourth quarter measured pressive 4.3% annual growth rate. 97, real GDP grew at the fastest n a decade, driven by healthy con- r spending and business invest-. But that should slow in 1998, BUSINESS WEEK's economists ex- real GDP to rise a more modest and capital spending, which hit

record levels last year, to slow. A 2.4% GDP jump would be the smallest gain in three years.

Even hot performers in 1997, such as Exxon Corp., won't be immune to these pressures for long. The oil giant, which posted the biggest profit of any company on the list in 1997, \$8.5 billion, benefited from the time lag between the drop in crude oil costs and a decline in gas prices at the pump. This year, falling pump prices are expected to close the lag and cool Exxon's returns.

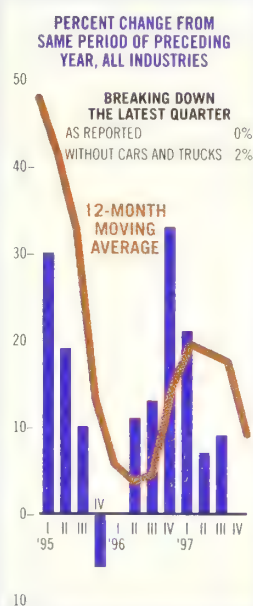
Nor will a broad economic drop-off be welcomed by industries that suffered in 1997. After a 116% runup in 1996 profits, phone companies fell fast in 1997. AT&T's new cost-cutting CEO, C. Michael Armstrong, didn't arrive soon enough to halt a 20% earnings drop. Problems in the consumer market hit AT&T and ri-

val MCI Communications Corp., says Anna-Maria Kovacs, an analyst with Janney Montgomery Scott Inc. MCI lost \$391 million in the fourth quarter and eked out a \$2 million profit for 1997.

INSURANCE COUP. The winning industries of 1997 included insurance, which saw the lowest catastrophic loss rate since 1988, a drop in car accidents, and healthy stock investment returns. Property and casualty giants like Allstate Corp. grew profits 50% and more, while Hartford Financial Services Group, which posted a \$99 million loss in 1996, turned in a \$1.3 billion profit in 1997. The upturn was due to stronger business lines and a windfall from the IPO of its Hartford Life business. The 1998 outlook isn't as rosy. "Among the few ways to increase earnings in '98 is to have even fewer catastrophes than in

A Spotlight On 1997 Profits

AFTERTAX PROFITS, QUARTER BY QUARTER

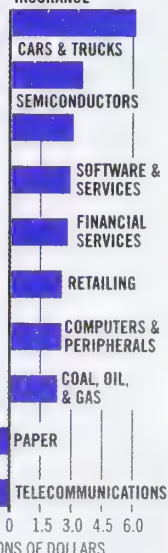


INDUSTRIES WITH THE BIGGEST DOLLAR CHANGE IN 1997

The long-expected weakening of earnings growth finally happened in 1997, as profits went from a 21% increase in the first quarter to a 0% gain in the fourth. For the year, profits rose only 9%, on a 9% revenue gain.

A profit turnaround at Hartford Financial Services helped make insurers winners. Strong results at Ford and GM paced the auto makers, while Intel followed last year's 45% profit leap with a 35% jump in 1997. Big charges at Champion International and Kimberly-Clark hurt the paper companies. Profits at AT&T dropped 20%. Margins slid to 5.5%, the lowest level since 1995's fourth quarter. A hint of problems to come?

CHANGE IN AFTERTAX PROFITS FROM 1996



Corporate Scoreboard

'97," says Harris R. Chorney, national director for insurance at KPMG Peat Marwick. Few would bet on that.

Detroit also had a big year. Slicing a huge \$3 billion in costs, Ford Motor Co. bested General Motors Corp. to post an industry-record \$6.9 billion profit. A long strike and a dearth of new products clipped Chrysler Corp., and the coming year is expected to challenge all three. Merrill Lynch analyst Nicholas Lobacaro predicts that lower demand for vehicles worldwide and pricing pressure from Asian imports will push earnings for the Big Three down 13%.

Semiconductor makers also rebounded smartly from a poor 1996, with profits up an impressive 48%. Memory-chip prices continued to drop for the second year running, but that was offset by sizzling microprocessor sales and volume growth. No surprise, Intel led the way back, posting 35% growth on the



Business' ability to raise prices is at a 35-year low

strength of its Pentium microprocessors. Strong demand from U.S. corporate buyers and a surge of orders from Europe helped PC manufacturers like Compaq Computer Corp. and Dell Com-

puter Corp. do well in 1997. But pressure could rise this year, as corporations start to clamor for the sub-\$100 models so popular now with consumers.

For many in the financial services industry, however, downtimes remain a distant fear. Fueled by low interest rates, the soaring stock market and a record year in M&A, financial companies continue to rake it in. Giant Morgan Stanley, Dean Witter, Discover & Co. saw earnings for the year rise 32% to \$2.6 billion, while Merrill Lynch & Co. earnings gained 18%, to \$1.9 billion. So far, 1998 is shaping up to be another big year for Wall Street. But back on Main Street, many face tougher going. "The process of growing earnings is harder in 1997," says economist Stephen L. Zepher. "and will get harder again in 1998. Finally, the predictions are playing out."

By Nanette Byrnes in New York with bureau reports

A KINK IN THE PROFITS PIPELINE

Last year's net profit gains of 9% may look disappointing, but by the end of 1998, Wall Street may well covet such growth. That's because a consensus forecast of 50 economists, taken by Blue Chip Economics, projects a rise in corporate profits of only 4.6% this year. The primary culprits: a slower economy and resurging labor costs.

The tight job market has emboldened workers either to switch jobs for more pay or to win fatter raises from their current bosses. Employment costs in the fourth quarter jumped 3.5% from a year ago. Of course, for most of this seven-year expansion, productivity gains offset pay hikes. So growth in unit labor costs stayed below price rises, letting companies widen profit margins.

But that was before the fourth quarter. Even though productivity surged 2% last quarter, it couldn't make up for a 2.9% boost in unit labor costs. Indeed, the labor cost hike was almost twice the 1.5% gain seen in the prices of goods and services bought in the U.S. That's why margins fell at year's end.

For 1998, the squeeze will likely get worse. First, even if economic growth slows to 2.4% this year as forecast by BUSINESS WEEK's economists, that pace will be rapid enough to create millions of new jobs and

push the joblessness rate lower than its current 4.7%. The ensuing dearth of highly skilled employees will give more workers an upper hand in pay deals. Moreover, talk in Washington of a minimum-wage hike in 1999 suggests that the upward pressure on pay will continue into next year.

At the same time, productivity will not repeat its 1.7% rise of 1997, says Chris Varvares of Macroeconomics Advisers. He argues that much of last year's rise was a cyclical response to a surge in demand and, with the economy slowing, output per hour worked will grow just 1.1% this year.

Moreover, pricing power will stay weak, especially for manufacturers whose products compete with suddenly cheaper imports. Helen Hotchkiss, senior economist at Dreyfus Corp., says industries selling direct to consumers will have the best chance of making markups stick. Because of the gain in buying power, she believes consumers may become less price sensitive in some areas. She points to America Online's recent 10% rise in monthly charges as a taste of things to come. Even so,

service companies may be hard-pressed to make a buck, because their labor bills are rising faster than manufacturers'.

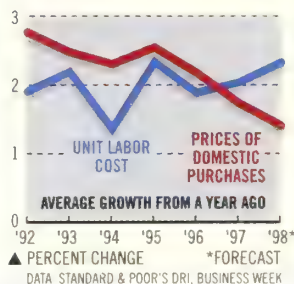
Still, all is not gloomy on the cost front. For one thing, the recent trucking contract signed by the Teamsters union calls for modest price

raises of 2.5% annually. This suggests that the bargaining edge enjoyed by select groups such as United Parcel Service workers has not spread into the broader labor force. And Varvares points out that more pay is linked to performance, so the slowdown in output and productivity this year will result in smaller bonuses

and benefits. A drop in nonlabor costs, such as energy, will also offset a piece of the labor tab.

In general, though, more companies in 1998 will warn about profit shortfalls because of rising labor costs. That's hardly startling, given the late stage of this expansion and the tightness of the labor markets. But expected or not, companies won't like delivering the bad news and investors won't like hearing it. By Kathleen Madigan in New York

LABOR COSTS OUTPACE PRICE HIKES



Fourth Quarter & Full Year 1997

CORPORATE SCOREBOARD

Summary

S: Includes all sales and operating revenues. For includes all operating revenues.

TS: Net income before extraordinary items. For banks,

profits are net income after security gains or losses.
MARGINS: Net income from continuing operations before extraordinary items as percent of sales.

RETURN ON COMMON EQUITY: Ratio of net income available

for common stockholders (most recent 12 months) to latest available common equity, which includes common stock, capital surplus, and retained earnings.

PRICE-EARNINGS RATIO: Based on Feb. 6, 1998, common-stock price and corporate earn-

ings from continuing operations before extraordinary items for most recent 12-month period.

EARNINGS PER SHARE: For most recent 12-month period. For most companies, this figure represents diluted earnings per share.

COMPANY

	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 12-31	PRICE- EARNINGS RATIO 2-6	12 MONTHS' EARNINGS PER SHARE
	4TH QUARTER 1997 \$ MIL.	CHANGE FROM 1996 %	12 MONTHS 1997 \$ MIL.	CHANGE FROM 1996 %	4TH QUARTER 1997 \$ MIL.	CHANGE FROM 1996 %	12 MONTHS 1997 \$ MIL.	CHANGE FROM 1996 %	4TH QUARTER 1997 %	4TH QUARTER 1996 %			
INDUSTRY COMPOSITE	1485777.0	9	5607745.0	9	81065.8	0	348309.6	9	5.5	5.9	16.5	25	2.16
AEROSPACE & DEFENSE													
INDUSTRY COMPOSITE	31489.5	10	118879.2	15	470.6	-64	3566.7	-27	1.5	4.6	11.7	35	1.77
ANT TECHSYSTEMS (9)	269.2	-11	1098.6	3	18.0	11	50.1	-10	6.7	5.4	24.2	16	3.73
IG	11727.0	18	45800.0	29	-498.0	NM	-178.0	NM	NM	4.5	-1.4	NM	-0.18
AL DYNAMICS	1101.0	23	4062.0	13	83.0	19	316.0	17	7.5	7.8	17.0	18	4.99
STREAM AEROSPACE	540.9	68	1903.5	79	44.4	209	243.0	417	8.2	4.5	586.8	11	3.13
NET INTERNATIONAL	306.2	8	1258.2	14	12.7	29	72.0	181	4.1	3.5	25.1	23	0.66
HEED MARTIN	7878.0	3	28069.0	4	371.0	-20	1300.0	-3	4.7	6.1	18.7	18	6.08
PROP GRUMMAN	2510.0	4	9153.0	6	117.0	388	407.0	54	4.7	1.0	16.3	22	5.98
STRAND	490.0	19	1752.0	15	55.0	175	188.0	65	11.2	4.9	34.7	18	3.13
OL (6) †	350.2	67	1070.1	24	23.5	26	96.6	59	6.7	8.9	17.9	17	5.10
D TECHNOLOGIES	6317.0**	3	24713.0	5	244.0	7	1072.0	18	3.9	3.7	25.5	20	4.21
AUTOMOTIVE													
INDUSTRY COMPOSITE	113794.8	8	431832.2	5	5039.3	85	18838.8	31	4.4	2.6	23.6	9	5.16
TRUCKS & TRUCKS													
JP COMPOSITE	99980.1	7	379102.7	5	4587.7	50	16917.6	26	4.6	3.3	25.0	8	5.90
SLER	16768.0	7	58622.0	-1	852.0	-15	2805.0	-25	5.1	6.4	24.7	9	4.09
MOTOR	39952.0	3	153626.9	5	1796.0	49	6920.0	56	4.5	3.1	23.1	9	5.62
AL MOTORS	39458.0**	10	153781.0	6	1737.0	121	6698.0	35	4.4	2.2	27.9	7	8.62
TAR INTERNATIONAL (2)	1929.0	34	6321.0	11	70.0	NM	150.0	131	3.6	0.0	15.6	17	1.83
AR	1873.2	47	6751.9	47	132.7	112	344.6	71	7.1	4.9	22.9	13	4.41
ARTS & EQUIPMENT													
JP COMPOSITE	9785.6	15	36938.9	11	348.1	1166	1118.1	49	3.6	0.3	15.6	20	2.03
INDUSTRIES	598.5	7	2349.0	6	17.3	-8	65.0	38	2.9	3.4	13.4	14	2.78
WARNER AUTOMOTIVE	467.0	11	1767.0	15	27.2	NM	103.2	147	5.8	NM	15.0	12	4.31
	2166.8**	13	8770.3	11	84.4	20	369.1	21	3.9	3.7	21.7	15	3.49
NT DIESEL	562.7	11	2163.9	10	7.9	72	29.9	687	1.4	0.9	8.7	16	1.21
N (4)	889.5	5	3607.1	10	32.6	-15	-52.5	NM	3.7	4.5	-5.6	NM	-0.83
AL-MOGUL	415.0	-14	1806.6	-11	12.2	NM	72.0	NM	2.9	NM	19.4	28	1.67
JRP (1)	443.2	9	1568.2	4	22.0	-6	137.4	230	5.0	5.7	48.8	8	3.36
LEMMEZ INTERNATIONAL (11)	369.8	58	1120.3	61	10.9	132	-47.4	NM	2.9	2.0	-29.6	NM	-2.27
	2143.7	25	7342.9	18	68.6	34	208.2	37	3.2	3.0	18.6	18	3.05
OR AUTOMOTIVE (3)	911.0	21	3464.0	10	32.0	28	116.0	-1	3.5	3.3	74.8	NA	NA
VE MFG. (9)	267.7	6	1028.8	3	17.8	16	70.6	15	6.7	6.1	17.5	15	2.33
ARD PRODUCTS (6)	282.5	6	1104.8	-1	8.8	38	31.4	3	3.1	2.4	11.7	16	1.87
SH NATIONAL	268.2	59	846.1	34	6.5	422	15.2	318	2.4	0.7	6.6	41	0.73
RE & RUBBER													
JP COMPOSITE	4029.1	4	15790.6	2	103.5	NM	803.1	176	2.6	NM	16.6	17	3.08
AG	256.0	26	822.5	9	66.9	208	122.0	50	26.1	10.7	25.9	10	5.33
R TIRE & RUBBER	488.9	17	1813.0	12	34.6	6	122.4	13	7.1	7.9	14.7	16	1.55
EAR TIRE & RUBBER	3284.2	0	13155.1	0	2.0	NM	558.7	449	0.1	NM	15.8	18	3.53

Fourth quarter ended Nov. 30. (2) Fourth quarter ended Oct. 31. (3) First quarter and most recent 12 months ended Dec. 31. (4) First quarter and most recent 12 months ended Nov. 30. (5) First quarter and most recent 12 months ended Oct. 31. (6) Second quarter and most recent 12 months ended Dec. 31. (7) Second quarter and most recent 12 months ended Nov. 30. (8) Second quarter and most recent 12 months ended Oct. 31. (9) Third quarter and most recent 12 months ended Dec. 31. (10) Third quarter and most recent 12 months ended Nov. 30. (11) Third quarter and most recent 12 months ended Oct. 31. (12) Fourth quarter ended Jan. 31. *Sales include excise taxes. **Sales include other income. ***Sales include excise taxes and other income. Sales from major subsidiaries not included in consolidated sales. Earnings per share are for latest 12 months, not necessarily for end of most recent fiscal year; they include all common-stock earnings but exclude extraordinary items. NA = not available. NM = not meaningful. DATA: STANDARD & POOR'S COMPUSTAT SERVICES, A DIVISION OF THE MCGRAW-HILL COMPANIES.

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 12-31	PRICE-EARNINGS RATIO 2-6
	4TH QUARTER 1997 \$ MIL.	CHANGE FROM 1996 %	12 MONTHS 1997 \$ MIL.	% CHANGE FROM 1996 %	4TH QUARTER 1997 \$ MIL.	CHANGE FROM 1996 %	12 MONTHS 1997 \$ MIL.	CHANGE FROM 1996 %	4TH QUARTER 1997 %	4TH QUARTER 1996 %		
3 BANKS												
INDUSTRY COMPOSITE	80349.7	11	308576.4	10	10021.1	8	39000.0	11	12.5	12.8	16.3	19
(A) BANKS - EAST												
GROUP COMPOSITE	37193.3	10	142791.6	10	4286.5	4	16731.4	14	11.5	12.2	17.7	17
BANK OF NEW YORK	1582.0	19	5697.0	0	298.0	19	1104.0	8	18.8	18.9	22.4	21
BANKBOSTON	1749.9	10	6727.2	8	234.7	16	897.2	38	13.4	12.7	19.6	17
BANKERS TRUST NEW YORK	3251.0	18	12176.0	15	207.0	13	866.0	13	6.4	6.7	16.2	14
CHASE MANHATTAN	7808.0	12	30381.0	11	874.0	5	3708.0	51	11.2	12.0	17.6	15
CITICORP	8999.0	5	34697.0	6	1061.0	8	3591.0	-5	11.8	11.5	17.9	17
FIRST MARYLAND BANCORP	372.8	54	1267.6	35	27.7	-23	151.2	14	7.4	14.9	7.7	NA
FLEET FINANCIAL GROUP	2000.0**	-1	8095.0	3	335.0	11	1303.0	14	16.8	15.0	19.5	16
MBNA	1216.6**	26	4523.9	38	188.3	26	622.5	31	15.5	15.4	32.3	29
MELLON BANK	1392.0**	10	5134.0	8	195.0	1	771.0	5	14.0	15.3	20.5	22
MORGAN (J. P.)	4496.0	6	17701.0	12	271.0	-35	1465.0	-7	6.0	9.9	13.4	16
PNC BANK	1785.3	11	6859.2	8	265.5	-2	1052.5	6	14.9	16.9	19.2	17
REPUBLIC NEW YORK	991.9**	15	3738.2	14	116.1	7	449.1	7	11.7	12.6	14.1	15
STATE STREET	933.0	27	3428.0	25	101.0	29	380.0	30	10.8	10.6	19.9	26
SUMMIT BANCORP.	615.8	12	2366.6	9	112.2	16	371.0	31	18.2	17.6	14.7	24
(B) BANKS - MIDWEST												
GROUP COMPOSITE	17293.0	9	66429.0	7	2588.8	15	8907.7	1	15.0	14.2	16.6	24
BANC ONE	3407.5**	3	13219.1	9	474.8	7	1305.7	-22	13.9	13.4	13.0	28
COMERICA	822.9	8	3175.4	3	139.9	130	530.5	27	17.0	7.9	20.4	30
FIFTH THIRD BANCORP	501.4**	10	1923.8	10	107.2	15	401.2	20	21.4	20.5	17.6	31
FIRST CHICAGO	2599.0	7	10098.0	0	382.0	1	1525.0	6	14.7	15.5	19.4	16
FIRST OF AMERICA BANK	521.5	-3	2077.9	0	83.1	-1	314.8	23	15.9	15.6	17.3	21
FIRSTAR	501.5**	8	1892.6	4	75.4	2	295.2	18	15.0	15.9	18.1	20
HUNTINGTON BANCSHARES	588.3	11	2324.3	11	90.6	15	292.7	-4	15.4	14.9	15.0	23
KEYCORP	1731.0	13	6568.0	9	248.0	64	919.0	17	14.3	9.9	18.1	16
MARSHALL & ISLEY	514.3**	28	1742.5	18	71.9	16	245.1	21	14.0	15.4	17.5	24
MERCANTILE BANCORPORATION	625.4	27	2256.9	19	94.8	17	204.6	-17	15.2	16.4	8.7	32
NORTHERN TRUST	609.1	24	2267.3	17	81.3	21	309.4	20	13.3	13.7	18.8	26
NORWEST	2503.5	7	9659.7	9	356.1	16	1351.0	17	14.2	13.1	19.5	22
OLD KENT FINANCIAL	335.0	11	1305.7	13	43.0	3	180.3	14	12.8	13.8	17.3	21
STAR BANC	263.6	13	1009.1	11	51.7	22	194.8	23	19.6	18.1	21.5	26
U. S. BANCORP	1769.0	6	6908.8	0	288.9	-1	838.5	-31	16.3	17.6	14.1	34
(C) BANKS - SOUTH & SOUTHEAST												
GROUP COMPOSITE	16020.6	18	60912.5	15	1860.2	-2	8270.6	17	11.6	14.1	15.4	19
BB&T	667.5	13	2597.9	14	103.4	29	359.9	9	15.5	13.5	17.3	24
CRESTAR FINANCIAL	520.3	11	1997.0	5	82.7	117	309.8	42	15.9	8.1	15.0	20
FIRST AMERICAN	268.3	12	1012.0	14	38.9	16	145.5	20	14.5	13.9	16.4	20
FIRST TENNESSEE NATIONAL	441.8	13	1609.4	10	57.9	9	197.5	10	13.1	13.7	21.7	21
FIRST UNION	3663.0	7	14329.0	9	362.0	-27	1896.0	17	9.9	14.4	17.0	17
NATIONSBANK	5788.0	34	21581.0	24	818.0	29	3077.0	30	14.1	14.6	15.1	16
POPULAR	475.4	23	1738.9	18	55.3	16	209.6	13	11.6	12.4	15.1	17
REGIONS FINANCIAL	504.2	22	1911.6	19	79.0	22	299.7	30	15.7	15.6	15.7	19
SOUTHTRUST	663.9	18	2502.8	22	82.0	20	306.7	20	12.3	12.2	14.0	20
SUNTRUST BANKS	1201.8	14	4585.0	13	172.2	9	667.3	8	14.3	15.0	13.4	23
UNION PLANTERS	445.2**	0	1778.3	3	5.3	-76	208.8	22	1.2	5.1	12.7	26
WACHOVIA	1381.2	10	5269.6	8	3.6	-98	592.8	-22	0.3	16.8	13.6	27
(D) BANKS - WEST & SOUTHWEST												
GROUP COMPOSITE	9842.9	5	38443.3	8	1285.6	27	5090.2	14	13.1	10.8	13.5	19
BANKAMERICA	6038.0	5	23585.0	7	812.0	9	3210.0	12	13.4	13.0	16.2	17
FIRST SECURITY	418.0	20	1503.4	17	55.3	8	205.9	16	13.2	14.7	15.6	21
PACIFIC CENTURY FINANCIAL	329.0	10	1250.4	9	33.1	-4	139.5	5	10.1	11.5	12.2	13
UNIONBANCAL	643.9	9	2496.5	6	87.1	63	379.8	69	13.5	9.0	15.4	13
WELLS FARGO	2414.0	2	9608.0	10	298.0	142	1155.0	8	12.3	5.2	8.9	25
4 CHEMICALS												
INDUSTRY COMPOSITE	35268.6	1	144833.5	3	1720.8	-5	9878.1	-8	4.9	5.2	18.8	22
AIR PRODUCTS & CHEMICALS (3)	1234.8	10	4751.7	14	160.5	61	489.9	15	13.0	8.9	18.5	19
ARCO CHEMICAL	1006.0	3	3995.0	1	65.0	2	111.0	-68	6.5	6.5	6.2	42
BETZDEARBORN	334.2	3	1294.8	25	25.8	127	92.2	43	7.7	3.5	20.3	22
CABOT (3)	435.4	9	1666.6	-8	31.5	25	99.1	-44	7.2	6.3	13.4	24
CROMPTON & KNOWLES	428.1	6	1851.2	3	8.9	346	92.1	NM	2.1	0.5	NM	24
CYTEC INDUSTRIES	359.5	14	1290.6	2	30.6	17	113.6	13	8.5	8.3	29.3	21
DOW CHEMICAL	4803.0**	-2	20018.0	0	358.0	-13	1808.0	-5	7.5	8.4	23.4	12
DUPONT	11330.0***	-1	45079.0	3	262.0	-69	2405.0	-34	2.3	7.5	21.0	29
EASTMAN CHEMICAL	1154.0	4	4678.0	-2	28.0	-53	286.0	-25	2.4	5.4	16.3	17
ETHYL	274.5	-10	1063.6	-7	16.2	-36	77.6	-17	5.9	8.3	17.3	10
FERRO	337.1	1	1381.3	2	16.1	16	-37.3	NM	4.8	4.2	-12.2	NM
FULLER (H. B.) (1)	350.4	5	1306.8	2	12.6	2	40.3	-11	3.6	3.7	12.0	19
GEON	312.3	12	1250.0	9	3.5	119	22.5	84	1.1	0.6	9.9	22

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 12-31	PRICE- EARNINGS RATIO 2-6	12 MONTHS' EARNINGS PER SHARE
	4TH QUARTER 1997 \$ MIL.	CHANGE FROM 1996 %	12 MONTHS 1997 \$ MIL.	CHANGE FROM 1996 %	4TH QUARTER 1997 \$ MIL.	CHANGE FROM 1996 %	12 MONTHS 1997 \$ MIL.	CHANGE FROM 1996 %	4TH QUARTER 1997 %	4TH QUARTER 1996 %			
AT LAKES CHEMICAL	325.7	14	1311.2	-3	-16.7	NM	71.8	-40	NM	5.1	4.9	39	1.19
NA (M.A.)	555.9	11	2200.3	6	15.6	6	64.6	9	2.8	2.9	12.0	16	1.40
CULES	421.0	-15	1866.0	-9	60.0	-21	324.0	0	14.3	15.4	41.0	15	3.18
GLOBAL	676.9	3	2988.6	2	-66.3	NM	87.8	-35	NM	7.4	4.5	36	0.93
ATIONAL FLAVORS & FRAGRANCES	306.3	-5	1426.8	-1	35.0	-15	218.2	15	11.4	12.6	21.1	22	1.99
RIZOL	423.5	13	1673.8	5	30.5	6	154.9	-9	7.2	7.6	19.0	14	2.66
DELL PETROCHEMICAL	535.0	-31	2878.0	9	51.0	-2	286.0	127	9.5	6.8	46.2	8	3.58
ENNIUM CHEMICALS	625.0	-18	3048.0	0	16.0	-58	185.0	31	2.6	5.0	12.6	10	2.47
SANTO	1820.0	26	7514.0	18	5.0	NM	294.0	-29	0.3	NM	7.2	NM	0.48
TON INTERNATIONAL (6)	664.9**	18	2519.6	13	58.2	15	230.3	26	8.8	9.0	11.8	20	1.65
CO CHEMICAL	373.7	10	1433.7	10	43.3	7	163.4	12	-11.6	11.9	23.8	19	2.10
	578.0	-2	2409.5	-9	34.5	-76	152.9	-47	6.0	24.6	17.4	15	3.00
KAIR	1209.0	5	4735.0	6	100.0	4	416.0	48	8.3	8.3	19.6	17	2.53
M & HAAS	950.0	-2	3999.0	0	98.0	31	410.0	13	10.3	7.8	24.3	14	6.39
JULMAN (A.) (4)	264.2	2	1002.8	2	12.5	5	51.3	12	4.7	4.6	13.0	18	1.40
ITIA	731.0	-5	2969.0	0	9.0	NM	192.0	500	1.2	NM	NM	18	1.55
RA INDUSTRIES	390.9**	7	2542.4	10	48.7	141	209.9	57	12.4	5.5	26.6	4	2.80
IN CARBIDE	1539.0	2	6502.0	6	147.0	44	676.0	14	9.6	6.8	29.0	10	4.53
CU	519.4	-4	2187.4	-3	20.8	NM	90.1	NM	4.0	NM	13.9	27	1.55
CONGLOMERATES													
INDUSTRY COMPOSITE	46571.0	14	166621.5	12	2757.3	-3	10975.5	7	5.9	7.0	20.6	31	2.05
GHENY TELEDYNE	920.9	0	3745.1	-2	82.9	28	297.6	31	9.0	7.1	29.8	15	1.70
EDSIGNAL	3910.0	12	14472.0	4	314.0	16	1170.0	15	8.0	7.7	26.5	20	2.02
GROUP (11)	373.1	136	1297.4	92	-23.2	NM	-39.4	NM	NM	NM	-54.8	NM	-19.31
ERAL ELECTRIC	26695.0**	16	90840.0	15	2350.0	14	8203.0	13	8.8	9.0	24.3	32	2.46
COURT GENERAL (2)	991.3**	14	3691.6	12	8.1	-86	-115.1	NM	0.8	6.7	-13.6	NM	-1.64
OFFICE SOLUTIONS (3)	1374.3	21	5362.3	24	37.0	-17	114.7	-34	2.7	3.9	8.0	47	0.71
INDUSTRIES	2299.1	3	8777.1	1	77.9	9	113.7	-50	3.4	3.2	13.8	35	0.92
MARK INTERNATIONAL	665.4	9	2406.8	6	20.8	-35	103.8	83	3.1	5.2	11.4	18	1.59
NECO	1868.0	11	7220.0	10	76.0	NM	361.0	66	4.1	NM	13.9	20	2.11
IRON	2818.0**	16	10544.0	14	150.0	17	558.0	16	5.3	5.3	17.0	20	3.29
	2798.5	14	10831.3	10	-410.8	NM	-48.5	NM	NM	4.5	-2.3	NM	-0.40
INDUSTRIES (3)	596.0	16	2366.0	14	24.0	14	116.0	29	4.0	4.1	16.6	18	1.55
	272.3	6	1093.0	2	39.2	NM	27.1	NM	14.4	NM	7.1	43	0.23
	610.6	8	2417.5	7	26.7	1	97.8	42	4.4	4.7	19.3	21	1.03
TMAN	378.6	6	1557.5	4	-15.3	NM	15.8	-67	NM	1.0	2.8	NM	0.15
CONSUMER PRODUCTS													
INDUSTRY COMPOSITE	77039.2	6	292072.2	6	5528.6	8	24197.6	13	7.2	7.1	27.7	28	1.90
APPAREL													
UP COMPOSITE	7339.1	6	29074.7	13	352.3	-17	1699.8	11	4.8	6.1	18.8	15	2.38
WN GROUP (11)	433.9**	3	1563.5	3	-13.3	NM	-6.9	NM	NM	3.1	-3.2	NM	-0.38
S APPAREL GROUP	349.2	33	1387.5	34	24.0	47	121.7	51	6.9	6.2	26.3	21	2.26
WOOD (8)	502.9	17	1667.6	14	16.5	14	41.1	44	3.3	3.4	11.1	17	1.89
(7)	2255.3	7	9818.9	26	141.0	-20	787.1	16	6.3	8.4	22.8	16	2.65
WEST GROUP (11)	496.6	12	1780.0	13	34.6	-2	88.5	55	7.0	8.0	19.8	11	2.40
LIPS-VAN HEUSEN (11)	413.6	6	1393.9	2	14.6	-3	-15.4	NM	3.5	3.8	-5.8	NM	-0.57
RALPH LAUREN (9)	405.7	22	1369.3	14	29.3	44	143.1	NA	7.2	6.1	NA	18	1.53
OK INTERNATIONAL	863.4	10	3643.6	5	0.6	-97	135.1	-3	0.1	2.6	26.6	12	2.32
SELL	331.5	-8	1228.2	-1	11.8	-60	54.4	-33	3.6	8.1	8.3	17	1.47
	1287.0	-7	5222.2	2	93.2	13	350.9	17	7.2	6.0	18.5	16	2.70
APPLIANCES & HOME FURNISHINGS													
UP COMPOSITE	12342.0	14	45285.4	8	359.0	235	1171.8	30	2.9	1.0	11.5	32	1.25
STRONG WORLD INDUSTRIES	527.4	0	2198.7	2	46.8	-13	185.0	12	8.9	10.2	22.6	16	4.50
BATH & BEYOND (10)	281.0	31	1006.8	34	18.9	36	66.6	35	6.7	6.5	24.8	41	0.95
BUY (10)	2106.4	5	7853.6	-2	26.4	NM	39.0	198	1.3	NM	8.2	61	0.89
UIT CITY GROUP (10)	1917.1	10	7693.2	8	14.0	-29	123.2	-18	0.7	1.1	7.8	30	1.24
ITURE BRANDS INTERNATIONAL	473.6	9	1808.3	7	18.9	8	67.1	24	4.0	4.0	20.7	23	1.15
O GUYS (3)	290.3	1	894.3	-1	2.4	22	-11.7	NM	0.8	0.7	-9.7	NM	-0.86
MAN INTERNATIONAL INDUSTRIES (6)	403.0	0	1467.0	1	16.0	-18	52.2	-10	4.0	4.9	11.1	16	2.80
IG-MEYERS (10)	678.5**	64	2313.2	59	-49.1	NM	-15.5	NM	NM	2.3	-2.4	NM	-0.26
BALL INTERNATIONAL (6)	264.5	4	1001.0	3	15.5	6	58.1	11	5.9	5.8	13.2	14	1.39
-BOY (8)	293.2	8	1037.6	7	16.8	10	44.0	6	5.7	5.6	12.1	18	2.45
ETT & PLATT	767.8	23	2909.2	18	55.1	23	208.3	36	7.2	7.1	18.6	23	2.16
NS 'N THINGS	283.4	23	874.2	26	16.9	38	25.8	72	6.0	5.3	9.2	35	1.30
TAG	945.1	22	3407.9	14	51.9	47	183.5	33	5.5	4.6	29.8	22	1.87
1 IMPORTS (10)	262.8**	16	1035.3	14	16.8	58	69.4	62	6.4	4.7	19.0	28	0.96
BEAM	338.1	26	1168.2	19	41.7	NM	123.1	NM	12.3	NM	23.1	26	1.41
RLPOOL	2510.0**	18	8617.0	1	50.0	25	-46.0	NM	2.0	1.9	-2.6	NM	-0.62
BEVERAGES													
UP COMPOSITE	17319.2	9	64938.4	7	1469.3	24	7192.7	22	8.5	7.4	34.7	37	1.42
EUSER-BUSCH	2507.4	1	11066.2	2	146.8	-2	1179.2	2	5.9	6.0	28.5	19	2.36
WN-FORMAN (8)	483.1	6	1617.4	3	60.9	10	176.6	9	12.6	12.1	22.6	21	2.56
ANDAIGUA BRANDS (10)	322.7	2	1191.8	6	17.6	112	45.9	213	5.5	2.6	11.5	24	2.37



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CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 12-31	PRICE- EARNINGS RATIO 2-6
	4TH QUARTER 1997 \$ MIL	CHANGE FROM 1996 %	12 MONTHS 1997 \$ MIL	CHANGE FROM 1996 %	4TH QUARTER 1997 \$ MIL	CHANGE FROM 1996 %	12 MONTHS 1997 \$ MIL	CHANGE FROM 1996 %	4TH QUARTER 1997 %	4TH QUARTER 1996 %		
COCA-COLA	4701.0	5	18868.0	1	817.0	7	4129.0	18	17.4	17.0	56.7	41
COCA-COLA ENTERPRISES	3049.0	44	11278.0	42	-19.0	NM	171.0	50	NM	0.4	9.5	76
PEPSICO	6256.0	3	20917.0	3	446.0	125	1491.0	58	7.1	3.3	23.5	37
(D) PERSONAL CARE												
GROUP COMPOSITE	19733.1	5	72582.7	5	2075.5	33	6838.0	20	10.5	8.3	31.5	35
ALBERTO-CULVER (3)	445.4	5	1794.6	8	19.7	-26	78.5	3	4.4	6.2	15.1	24
AVON PRODUCTS	1517.4	2	5079.4	6	133.7	1	338.8	7	8.8	8.8	149.3	26
CLOROX (6)	591.8**	12	2652.7	13	49.5	13	263.9	12	8.4	8.3	24.5	31
COLGATE-PALMOLIVE	2311.5	1	9056.7	4	206.4	14	740.4	17	8.9	7.9	33.7	34
DIAL	362.8	4	1362.6	-3	22.6	37	83.7	180	6.2	4.7	26.1	24
ESTEE LAUDER (6)	1000.9	6	3468.8	5	85.3	22	222.1	25	8.5	7.4	30.5	35
GILLETTE	3160.2	5	10062.1	4	470.9	308	1427.2	50	14.9	3.8	28.4	40
PROCTER & GAMBLE (6)	9641.0	5	36715.0	4	1046.0	11	3625.0	12	10.9	10.3	29.7	34
REVLON	702.1	14	2390.9	10	41.4	32	58.5	136	5.9	5.1	NM	39
(E) TOBACCO												
GROUP COMPOSITE	20305.9	1	80190.9	3	1272.5	-31	7295.2	-2	6.3	9.2	28.4	18
PHILIP MORRIS	13740.0	3	56114.0	3	1295.0	-12	6310.0	0	9.4	11.0	42.3	17
RJR NABISCO HOLDINGS	4583.0	-1	17057.0	0	-176.0	NM	402.0	-34	NM	4.6	3.7	31
STANDARD COMMERCIAL (9)	367.0	-2	1375.3	3	8.6	92	23.8	33	2.3	1.2	16.8	8
UNIVERSAL (6)	1265.2**	-5	4242.9	10	38.1	21	120.3	41	3.0	2.3	23.1	12
UST	350.8*	2	1401.7	2	106.8	-7	439.1	-5	30.5	33.2	111.0	15
7 CONTAINERS & PACKAGING												
INDUSTRY COMPOSITE	9404.2	6	38054.1	5	-21.6	NM	662.6	-42	NM	1.2	6.5	51
(A) GLASS, METAL & PLASTIC												
GROUP COMPOSITE	4003.5	7	17053.0	8	95.9	167	682.9	191	2.4	NM	13.5	21
BALL	574.8	15	2388.5	9	7.8	NM	58.3	345	1.4	NM	9.1	18
CROWN CORK & SEAL	1929.4	-2	8494.6	2	45.3	16	301.6	NM	2.3	0.0	9.2	24
OWENS-ILLINOIS	1138.2	18	4658.5	21	39.1	71	272.4	43	3.4	2.4	21.4	19
SILGAN HOLDINGS	361.1	11	1511.4	8	3.7	NM	50.6	65	1.0	0.1	NM	11
(B) PAPER												
GROUP COMPOSITE	5400.7	6	21001.1	2	-117.5	NM	-20.3	NM	NM	1.4	-0.7	NM
AVERY DENNISON	836.4	3	3345.7	4	54.4	14	204.8	16	6.5	5.9	24.5	25
BEMIS	454.9	5	1877.2	13	34.3	14	107.6	6	7.5	6.9	16.8	23
JEFFERSON SMURFIT	843.0	3	3238.0	-5	4.0	-73	1.0	NM	0.5	1.8	NM	NM
ROCK-TENN (3)	316.5	52	1217.9	41	8.7	17	17.4	-63	2.7	3.6	4.6	35
SONOCO PRODUCTS	736.4	2	2847.8	2	-126.6	NM	2.6	-98	NM	5.6	-0.1	NM
STONE CONTAINER	1285.3	3	4849.1	-6	-101.7	NM	-404.5	NM	NM	NM	NM	NM
TEMPLE-INLAND	928.2	10	3625.4	5	9.4	-49	50.8	-62	1.0	2.2	2.5	62
8 DISCOUNT & FASHION RETAILING												
INDUSTRY COMPOSITE	123235.0	12	480309.6	12	3205.8	0	13053.5	24	2.6	2.9	13.5	29
AMES DEPARTMENT STORES (11)	527.6**	2	2170.8	2	3.5	736	25.7	181	0.7	0.1	21.5	13
AUTOZONE (4)	675.3	19	2797.6	19	47.5	25	204.6	20	7.0	6.7	18.1	22
BARNES & NOBLE (11)	614.8	15	2710.8	18	0.1	NM	56.8	NM	0.0	NM	12.0	39
BJ'S WHOLESALE CLUB (11)	762.4	9	3095.8	10	13.8	43	61.7	26	1.8	1.4	14.9	NA
BORDERS GROUP (11)	477.3	15	2134.2	12	0.4	NM	67.6	NM	0.1	NM	13.3	40
BRADLEES (11)	333.7**	-18	1356.9	-20	0.4	NM	-107.6	NM	0.1	NM	NM	NM
BRYLANE (11)	365.5	131	1207.3	91	16.8	130	43.2	32	4.6	4.6	31.3	NA
BURLINGTON COAT FACTORY (6)	778.2**	5	1822.0	7	70.4	7	61.5	32	9.0	8.9	12.0	12
CALDOR (11)	562.9	-1	2529.7	-6	-35.1	NM	-155.1	NM	NM	NM	NM	NM
CARSON PIRIE SCOTT (11)	281.7**	6	1158.5	6	5.4	NM	38.2	10	1.9	NM	10.7	NA
CDW COMPUTER CENTERS	350.7	34	1276.9	38	13.9	30	51.0	48	4.0	4.1	25.5	26
COLE NATIONAL (11)	262.9	79	1008.3	63	2.7	130	-22.5	NM	1.0	0.8	-16.2	NM
CONSOLIDATED STORES (11)	669.8	12	3084.7	58	3.2	207	106.4	129	0.5	0.2	15.4	30
CORPORATE EXPRESS (10)	1064.2	12	3948.7	30	14.8	31	51.6	142	1.4	1.2	6.5	27
COSTCO (4)	5429.8**	11	22420.8	12	97.9	208	378.3	64	1.8	0.7	14.7	27
DAYTON HUDSON (11)	6622.0**	9	26971.0	7	179.0	53	661.0	36	2.7	1.9	15.6	27
DILLARD'S (11)	1639.3**	6	6681.4	5	44.3	40	258.0	65	2.7	2.0	9.4	16
DOLLAR GENERAL (11)	649.4	28	2441.4	21	33.6	26	131.2	28	5.2	5.2	25.0	42
FAMILY DOLLAR STORES (4)	542.7	19	2082.8	17	24.3	40	81.6	29	4.5	3.8	15.8	36
FEDERATED DEPARTMENT STORES (11)	3746.3**	4	15643.1	1	105.1	151	484.7	119	2.8	1.2	10.0	20
FINGERHUT	649.3	2	1798.6	2	43.9	39	69.3	73	6.8	5.0	10.3	16
GAP (11)	1765.9	28	6010.2	17	164.5	23	489.5	12	9.3	9.7	33.2	35
GLOBAL DIRECTMAIL	352.7	39	1145.4	26	12.9	9	38.8	-11	3.7	4.7	15.0	20
HILLS STORES (11)	434.6	-6	1796.0	-6	-3.9	NM	-32.8	NM	NM	NM	-16.7	NM
HOME DEPOT (11)	6217.0	26	23383.1	28	235.9	7	1103.8	27	3.8	4.5	16.2	42
HOMEBASE (11)	368.4	1	2327.8	5	-10.3	NM	28.7	-35	NM	1.2	7.9	9
INTIMATE BRANDS (11)	690.0	16	3381.4	20	35.4	30	287.1	24	5.1	4.6	66.2	25
KMART (11)	7315.0	1	32108.0	1	18.0	125	299.0	NM	0.2	0.1	5.7	22
KOHL'S (11)	757.8	27	2829.2	26	32.5	48	120.6	30	4.3	3.7	13.8	47
LANDS' END (11)	318.6	11	1206.5	10	8.2	33	60.3	54	2.6	2.1	28.8	23
LIMITED (11)	2070.6	4	8886.7	5	79.7	-50	345.5	21	3.8	8.0	17.4	23
LOWE'S (11)	2530.5	15	9780.8	18	88.1	17	340.6	24	3.5	3.4	13.4	28

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 12-31	PRICE- EARNINGS RATIO 2-6	12 MONTHS' EARNINGS PER SHARE
	4TH QUARTER 1997 \$ MIL	CHANGE FROM 1996 %	12 MONTHS 1997 \$ MIL	CHANGE FROM 1996 %	4TH QUARTER 1997 \$ MIL	CHANGE FROM 1996 %	12 MONTHS 1997 \$ MIL	CHANGE FROM 1996 %	4TH QUARTER 1997 %	4TH QUARTER 1996 %			
DEPARTMENT STORES (11)	2969.0**	4	12494.0	6	120.0	2	757.0	5	4.0	4.1	21.4	19	2.93
ANTIQUE STORES (11)	753.7**	4	3118.1	2	22.7	-27	120.0	-12	3.0	4.3	7.6	19	3.26
Y (FRED) (11)	1460.4	75	4607.1	25	18.3	190	78.3	57	1.3	0.8	6.1	27	1.32
EL'S STORES (11)	350.1	12	1443.1	8	4.4	NM	12.9	NM	1.3	NM	3.2	63	0.52
N MARCUS GROUP (5)	580.5**	7	2246.3	6	32.6	5	92.9	12	5.6	5.7	15.8	19	1.86
STROM (11)	1117.6**	10	4827.0	7	36.1	6	169.9	7	3.2	3.3	11.4	25	2.17
MAX (11)	992.4	15	3623.9	19	31.4	33	79.8	18	3.2	2.8	7.1	24	0.64
SS CASHWAYS (1)	504.4	-29	2285.3	-14	-335.0	NM	-421.8	NM	NM	0.8	NM	NM	NM
SS SHOESOURCE (11)	635.7	10	2520.3	7	33.5	14	126.6	110	5.3	5.1	15.5	21	3.25
Y (J.C.) (11)	7440.0**	30	29211.0	33	113.0	-52	436.0	-45	1.5	4.1	5.9	42	1.61
YS-MANNY, MOE & JACK (11)	525.6	10	1998.6	11	24.1	-13	100.1	3	4.6	5.8	11.8	15	1.58
ART (11)	441.5	20	1737.3	26	0.2	-98	-28.7	NM	0.0	2.8	-8.6	NM	-0.26
TT'S (11)	607.1**	31	2383.1	45	10.2	-16	42.6	555	1.7	2.6	6.2	42	0.74
STORES (11)	482.9	20	1926.2	18	25.1	53	108.8	55	5.2	4.1	33.1	16	2.15
HOLDINGS (11)	546.6**	15	2121.5	13	30.3	91	75.4	316	5.5	3.3	13.5	20	1.18
ROEBUCK	13149.0	9	41469.0	8	536.0	-5	1188.0	-7	4.1	4.7	22.0	17	2.99
DE MERCHANDISE	1442.9	-12	3662.8	-7	58.2	-26	-89.0	NM	4.0	4.8	-26.4	NM	-0.89
DO STORES (10)	608.4	3	2507.2	14	11.9	9	47.7	14	2.0	1.9	12.9	17	1.55
S AUTHORITY (11)	341.2	16	1423.5	17	2.0	2	31.0	18	0.6	0.7	9.5	13	0.98
STORES (11)	274.3	50	952.0	26	3.7	NM	27.8	127	1.3	NM	15.0	36	1.13
ES (11)	1414.2	31	4795.1	27	43.5	36	113.6	20	3.1	3.0	13.2	42	0.45
TS (11)	256.0**	3	1044.6	3	11.2	-44	32.7	-46	4.4	8.0	7.8	15	1.00
1)	1887.7	10	7092.7	11	106.9	31	283.5	94	5.7	4.7	26.0	22	1.59
R' US (11)	2141.9	14	10722.5	9	45.7	37	494.7	260	2.1	1.8	12.0	16	1.76
FFICE PRODUCTS (8)	952.4	20	3326.4	47	28.0	34	76.2	32	2.9	2.6	8.6	26	0.71
CITY DEPARTMENT STORES (5)	271.5	0	1094.3	7	3.3	-43	1.5	-94	1.2	2.1	0.6	NM	0.04
RE STORES (11)	286.3**	-13	1404.1	-12	-26.4	NM	-192.1	NM	NM	NM	NM	NM	-10.65
OFFICE PRODUCTS (6)	363.3	15	1382.8	17	19.9	20	75.2	12	5.5	5.2	20.3	28	0.87
ART STORES (11)	28777.0	12	113428.0	12	792.0	16	3334.0	15	2.8	2.7	19.0	29	1.47
WORTH (11)	1583.0	-12	6990.0	-6	55.0	-29	198.0	NM	3.5	4.3	17.2	15	1.46
5)	252.5	9	1275.6	11	1.0	NM	52.7	24	0.4	NM	9.6	18	1.43

ELECTRICAL & ELECTRONICS

STRY COMPOSITE	51138.7	10	191285.9	11	3048.8	-17	16179.8	27	6.0	7.9	15.8	26	2.21
ELECTRICAL PRODUCTS													
P COMPOSITE	7528.5	4	30187.9	4	550.8	9	2130.8	20	7.3	6.9	17.4	19	2.94
R INDUSTRIES	1288.1	-3	5288.8	0	108.9	24	394.6	25	8.5	6.6	15.6	17	3.26
	1934.0	12	7563.0	9	183.0	177	464.0	33	9.5	3.8	20.8	16	5.93
AL SIGNAL	433.7	-21	1954.6	-5	36.3	-7	131.0	-2	8.4	7.1	20.8	15	2.60
ILL	349.5	6	1378.8	6	10.9	-71	130.3	-8	3.1	11.2	15.4	27	1.89
ETEK (6)	298.5	2	1190.4	0	9.0	56	35.1	NM	3.0	2.0	21.8	17	1.17
NAL SERVICE INDUSTRIES (4)	487.6	-5	2011.8	-1	26.7	7	109.1	6	5.5	4.9	17.3	21	2.44
EM (6)	467.1	6	1815.5	5	56.0	7	245.7	14	12.0	11.9	29.3	14	2.75
WELL INTERNATIONAL (3)	1979.0	7	7888.0	6	89.0	-42	474.0	5	4.5	8.3	11.3	24	2.47
INTERNATIONAL	291.0	23	1097.0	16	31.0	-16	147.0	1	10.7	15.6	237.1	12	3.07
ELECTRONICS													
P COMPOSITE	17451.4	14	61886.6	11	431.3	-23	2785.4	7	2.5	3.7	7.8	33	1.57
S (6)	970.0	3	3917.5	5	52.7	16	220.2	17	5.4	4.8	13.6	17	2.75
ES ELECTRONICS	1694.6	39	5128.3	28	22.7	-21	406.3	139	1.3	2.4	0.3	34	1.07
I INDUSTRIES (5)	1039.0	-1	4165.7	9	43.4	9	165.6	8	4.2	3.8	15.2	17	3.49
ROLA	8278.0	8	29794.0	7	321.0	35	1180.0	2	3.9	3.1	9.0	33	1.94
OMM (3)	785.9	102	2493.3	136	36.8	303	119.6	497	4.7	2.3	11.1	29	1.63
EDON	4004.3	18	13673.5	11	-77.3	NM	526.8	31	NM	5.2	10.5	25	2.20
R	334.8	1	1265.7	17	12.3	27	44.4	21	3.7	2.9	17.1	17	1.65
N ASSOCIATES (3)	344.8	7	1448.7	-8	19.7	54	122.4	12	5.7	4.0	23.3	14	3.89
INSTRUMENTS													
P COMPOSITE	7511.2	15	27641.2	11	225.5	-59	1758.0	-8	3.0	8.4	15.3	29	2.03
MAN INSTRUMENTS	423.9	49	1198.0	17	-320.2	NM	-264.4	NM	NM	8.2	-66.5	NM	-9.58
ION ELECTRIC (3)	3171.5	12	12639.5	11	282.3	11	1149.3	10	8.9	9.0	21.2	25	2.59
'WELL	2325.8	10	8027.5	10	178.1	16	471.0	17	7.7	7.2	20.0	21	3.71
INCOR (6)	326.4	35	1167.3	32	52.1	52	139.4	6	16.0	14.1	12.2	26	1.59
N-ELMER (6)	342.9	4	1309.5	8	8.2	-84	64.0	13	2.4	15.4	14.1	45	1.42
ONIX (7)	529.0	11	2033.1	10	-21.2	NM	71.1	-29	NM	5.5	9.4	31	1.43
YNE	391.7	62	1266.3	8	46.2	NM	127.6	36	11.8	1.2	13.6	29	1.48
SEMICONDUCTORS & OTHER COMPONENTS													
P COMPOSITE	18647.6	8	71570.1	13	1841.3	-10	9505.6	48	9.9	11.9	21.0	25	2.37
ICED MICRO DEVICES	613.2	23	2356.4	21	-12.3	NM	-21.1	NM	NM	NM	-1.0	NM	-0.15
	1451.5	3	5745.0	5	127.0	NM	457.5	59	8.8	NM	15.6	20	2.08
G DEVICES (2)	332.5	9	1243.5	4	51.0	16	178.2	4	15.3	14.5	16.4	28	1.04
)	319.7	10	1263.2	13	33.3	11	135.7	7	10.4	10.4	17.1	14	1.54
	6507.0	1	25070.0	20	1743.0	-9	6945.0	35	26.8	29.7	36.0	23	3.87
CIRCUIT (4)	319.5	57	1094.5	31	19.1	116	62.7	124	6.0	4.3	31.3	28	1.63
GIC	323.0	7	1290.3	4	32.2	5	160.7	9	10.0	10.2	10.3	22	1.12
ELECTRONIC MATERIALS	258.6	28	986.7	-12	-3.5	NM	-6.7	NM	NM	NM	-1.0	NM	0.16

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CORPORATE SCOREBOARD

COMPANY	SALES			PROFITS			MARGINS				RETURN ON COMMON EQUITY 12 MONTHS ENDING 12-31	PRICE/EARNINGS RATIO
	1997 \$ MIL	1997 % CHG	12 MONTHS ENDING 1997 \$ MIL	1997 \$ MIL	1997 % CHG	4TH QUARTER 1997 \$ MIL	1997 % CHG	4TH QUARTER 1997 %	4TH QUARTER 1997 %			
MICRON TECHNOLOGY (4)	354.6	31	3742.0	17	9.6	-53	321.2	12	1.0	2.8	11.1	25
MOLEX (4)	412.5	2	1618.8	13	45.6	13	180.7	19	11.2	10.7	14.8	26
NATIONAL SEMICONDUCTOR (7)	719.9	5	2582.1	3	28.9	11	298.6	NM	4.0	3.8	14.0	12
READ-RITE	261.7	4	1171.8	24	-90.9	NM	-5.7	NM	NM	2.3	-4.5	NM
SCI SYSTEMS (6)	736.5	21	6392.6	19	37.6	27	132.0	34	2.1	2.0	20.9	24
SOLETRON (4)	35.2	41	4023.5	37	44.9	43	171.5	45	3.9	3.9	17.5	31
TEXAS INSTRUMENTS	2428.0	1	9750.0	2	263.0	NM	302.0	NM	NM	NM	4.8	71
THOMAS & BETTS	254.1	6	2114.7	7	45.9	NM	154.9	159	8.6	NM	15.8	18
VISHAY INTERTECHNOLOGY	253.5	16	1355.2	2	7.5	NM	53.3	1	NM	2.5	5.5	25
10 FOOD												
INDUSTRY COMPOSITE	90535.5	6	338465.2	5	1127.5	55	7188.5	-17	1.2	2.9	17.3	41
(A) FOOD DISTRIBUTION												
GROUP COMPOSITE	11659.8	5	41238.2	4	74.5	-54	644.9	14	0.6	1.4	14.4	21
ANDERSON'S	398.6	23	293.7	14	5.4	2	4.1	-36	1.4	1.7	5.6	18
INTERNATIONAL MULTIFOODS (10)	676.8	2	2611.4	1	9.4	5	6.5	64	1.4	1.2	2.1	29
JP FOODSERVICE (4)	177.3	2	177.3	NM	70.6	NM	NM	NA	NM	0.7	NM	NA
PERFORMANCE FOOD GROUP	332.4	4	1230.1	57	3.5	16	13.2	21	1.0	1.4	11.0	19
RICHFOOD HOLDINGS (8)	719.5	3	3377.2	4	15.6	19	65.9	49	2.1	1.7	22.9	20
SMART & FINAL	368.6	20	1453.0	12	-12.0	NM	6.6	73	NM	1.9	3.2	62
SUPERVALU (10)	4004.6	3	16793.4	2	40.2	0	232.1	36	1.0	1.0	19.5	12
SYSCO (6)	3786.1	5	14779.4	5	83.6	9	316.4	9	2.2	2.1	22.5	26
(B) FOOD PROCESSING												
GROUP COMPOSITE	40118.0	2	152550.9	3	525.2	-71	4435.5	-24	1.3	4.6	15.7	48
BESTFOODS	177.3	3	8400.4	-1	169.1	0	438.8	23	8.0	7.8	22.1	36
CAMPBELL SOUP (5)	2120.0	3	8032.0	4	267.0	203	282.5	33	12.6	4.3	59.3	29
CONAGRA (7)	6433.6	2	23828.5	-1	210.6	12	652.3	199	3.3	2.8	25.5	23
DEAN FOODS (7)	772.0	0	3034.0	3	26.6	39	97.8	NM	3.4	2.5	16.0	24
DOLE FOOD	665.1	22	433.1	1	23.2	NM	160.2	80	2.1	NM	24.6	19
EARTHGRAINS (3)	176.7	2	1662.2	1	14.1	53	32.2	425	2.7	1.8	5.5	30
FLOWERS INDUSTRIES (6)	404.6	6	1442.1	4	21.9	78	66.5	41	5.4	3.2	19.0	30
GENERAL MILLS (7)	1736.1	5	5788.4	4	64.6	-59	389.8	-13	3.9	10.0	100.2	30
HEINZ (H.J.) (8)	2264.1	5	9251.5	1	188.9	6	377.0	-45	8.3	7.4	15.4	57
HERSHEY FOODS	1242.4	4	4302.2	8	116.1	48	336.3	23	9.3	6.6	43.4	29
HORMEL FOODS (2)	868.1	1	3256.6	5	44.7	42	109.5	38	5.1	3.4	13.6	24
IBP	1279.1	8	13258.8	6	21.7	19	117.0	41	0.7	0.6	9.5	17
IMPERIAL HOLLY (3)	434.9	129	1010.3	41	0.1	NM	1.2	95	NM	0.8	6.6	10
INTERSTATE BAKERIES (7)	776.1	2	3218.3	1	34.2	31	116.4	102	4.5	3.5	21.8	24
KELLOGG	1617.7	4	6454.1	2	32.6	63	564.0	6	2.0	5.6	56.5	32
LANCASTER COLONY (6)	773.2	14	598.2	10	29.0	14	94.9	16	9.6	9.8	24.8	19
MCCORMICK (1)	557.0	4	1804.5	4	48.2	5	97.4	124	8.7	8.5	24.8	23
NABISCO HOLDINGS	2435.0	2	8734.0	2	172.0	56	431.0	NM	7.1	4.4	10.3	28
PILGRIM'S PRIDE (3)	347.5	13	1317.7	13	11.1	10	42.0	567	3.3	3.4	21.8	10
QUAKER OATS	1047.8	2	1555.7	4	25.6	41	930.9	NM	2.4	1.7	NM	NM
RALSTON PURINA (3)	317.1	5	4043.6	2	177.0	20	348.5	74	9.4	9.1	36.6	30
SARA LEE (6)	1773.5	0	19751.0	3	1278.0	NM	567.0	NM	NM	6.0	-14.1	NM
SMITHFIELD FOODS (2)	982.7	1	3098.7	4	15.5	73	44.2	61	1.6	0.9	13.8	30
STARBUCKS (3)	117.1	33	1044.8	36	22.1	54	65.1	39	7.0	6.0	12.2	50
TYSON FOODS (3)	1520.8	0	6348.6	-1	44.9	1	186.1	111	3.0	2.9	11.2	22
WRIGLEY (WM.) JR.	491.4**	5	1954.2	6	62.6	15	271.6	18	12.7	11.6	27.1	32
(C) FOOD RETAILING												
GROUP COMPOSITE	38757.8	10	144676.1	7	527.7	0	2108.2	-4	1.4	1.5	23.9	32
ALBERTSON'S (7)	3612.0	7	14475.9	7	123.4	16	496.4	1	3.4	3.2	21.8	24
AMERICAN STORES (11)	4647.5	2	10682.5	1	60.3	20	248.6	28	1.3	1.7	11.2	26
BRUNO'S (11)	610.1	12	2693.1	4	66.0	NM	87.7	NM	NM	NM	NM	NM
DOMINICK'S SUPERMARKETS (2)	568.5	4	2584.9	3	53.6	NM	38.9	NM	NM	NM	-33.4	NM
GENERAL NUTRITION (11)	278.0	33	1132.9	20	23.9	34	88.6	205	8.6	7.9	44.9	35
GIANT FOOD (10)	177.1	2	6011.6	2	12.2	35	52.5	53	1.3	2.1	6.0	38
GRAND UNION (7)	177.1	1	2276.5	2	45.8	NM	259.2	NM	NM	NM	NM	NM
GREAT ATLANTIC & PACIFIC TEA (10)	177.1	5	10106.8	0	11.2	20	73.3	3	0.5	0.6	7.9	15
HANNAFORD BROTHERS	870.7	14	3226.4	9	1.4	93	59.6	21	0.2	2.8	9.8	29
INGLES MARKETS	403.0	6	1557.9	4	1.2	46	18.0	15	0.7	1.4	8.1	15
KROGER	6509.5	5	26567.3	6	147.1	17	444.0	26	2.3	2.0	NM	24
PENN TRAITT	726.2**	2	3074.4	19	1.5	NM	54.6	NM	NM	NM	NM	NM
QUALITY FOOD CENTERS	677.5	2	1878.1	133	13.7	59	40.0	57	2.1	3.3	11.4	34
RUDDICK (3)	117.1	2	117.1	7	17.9	4	48.1	4	1.9	2.0	12.4	18
SAFEWAY	7785.4	42	22483.8	30	13.9	42	621.5	35	2.8	2.8	32.3	77
SOUTHLAND	777.7	2	7050.6	2	5.4	66	70.0	22	0.3	0.9	NM	13
SUPERMARKETS GENERAL HOLDING (11)	901.0	1	3710.7	3	11.5	NM	36.3	NM	NM	NM	NM	NA
WEIS MARKETS	470.3	2	1818.8	4	21.6	7	78.2	1	4.6	4.4	9.3	19
WHOLE FOODS MARKET (3)	407.8	30	1212.6	21	12.0	101	32.7	NM	3.0	1.9	15.9	42
WINN-DIXIE STORES (6)	177.1	2	13382.3	2	56.1	18	213.4	8	1.4	1.2	15.7	35

PORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 12-31	PRICE-EARNINGS RATIO 2-6	12 MONTHS' EARNINGS PER SHARE
	4TH QUARTER 1997 \$ MIL	CHANGE FROM 1996 %	12 MONTHS 1997 \$ MIL	CHANGE FROM 1996 %	4TH QUARTER 1997 \$ MIL	CHANGE FROM 1996 %	12 MONTHS 1997 \$ MIL	CHANGE FROM 1996 %	4TH QUARTER 1997 %	4TH QUARTER 1996 %			
AL													
RY COMPOSITE	127414.4	-8	499853.4	0	7768.6	5	31353.4	13	6.1	5.3	17.6	18	3.17
L, OIL & GAS													
COMPOSITE	117313.5	-10	463440.1	-2	6729.3	1	27914.3	9	5.7	5.1	17.6	17	3.40
HESS	2143.8**	-6	8340.0	-7	-61.4	NM	7.5	-99	NM	5.2	0.2	NM	0.08
	8186.0	-10	31910.0	1	789.0	-9	2720.0	-4	9.6	9.5	16.7	15	5.54
	318.9**	5	1176.3	20	45.5	-11	154.9	28	14.3	16.8	9.6	20	1.71
	342.5	70	1066.9	38	21.1	128	30.3	-8	6.2	4.6	5.0	26	1.00
AL													
(3)	3348.0	1	13352.0	7	52.0	117	221.0	73	1.6	0.7	9.9	18	2.90
RICHFIELD	450.0	-12	18684.0	1	382.0	1	1889.0	14	8.5	7.4	21.7	13	5.77
ON RESOURCES	541.0	-8	2000.0	-9	36.0	-74	319.0	-5	6.7	23.6	12.9	25	1.79
	8386.0	-15	35009.0	-7	875.0	89	3256.0	25	10.4	4.7	19.1	15	5.03
	2224.7	-28	9611.1	-19	131.2	-55	392.1	-22	5.9	9.5	11.8	17	3.49
	30813.0**	-8	122089.0	2	2500.0	0	8460.0	13	8.1	7.4	19.5	18	3.37
	1202.2	12	4462.5	9	3.6	-91	126.4	-18	0.3	3.6	9.7	15	4.05
	429.5	-17	1711.4	-11	45.2	-24	193.8	-12	10.5	11.4	13.5	16	4.04
EE													
	1079.9**	5	3847.5	15	3.9	-91	109.4	-16	0.4	4.1	16.6	24	1.97
	16332.0**	-29	65709.0	-19	704.0	4	3272.0	10	4.3	2.9	16.8	18	4.00
	565.4**	-2	2137.8	6	31.9	-21	132.4	5	5.6	7.0	12.4	17	2.94
IL PETROLEUM	1934.0	-3	8016.0	0	-178.0	NM	217.0	-58	NM	5.8	5.6	67	0.39
REGY	301.0**	-16	1197.0	4	41.0	-35	172.0	6	13.6	17.6	159.3	15	1.63
	698.0**	15	2654.3	7	61.0	114	180.3	35	8.7	4.7	15.8	18	3.76
PETROLEUM	3713.0	-15	15210.0	-3	209.0	5	959.0	-26	5.6	4.6	20.3	12	3.61
TATE	277.0	-4	1194.0	7	-24.6	NM	-7.4	NM	NM	NM	-2.3	NM	-0.21
	2545.0***	-16	10531.0	-7	29.0	NM	263.0	NM	1.1	NM	28.5	15	2.70
	12049.0**	-6	46667.0	3	623.0	22	2664.0	32	5.2	4.0	23.2	11	4.87
	3916.3	42	13281.6	34	41.1	36	212.7	45	1.0	1.1	11.1	26	1.37
DIAMOND SHAMROCK	3304.7*	21	10882.5	7	29.2	NM	159.7	NM	0.9	NM	9.1	18	1.94
SIFIC RESOURCES GROUP	480.4	-15	1905.7	4	74.2	-35	333.0	4	15.4	20.2	18.9	17	1.33
	1557.0**	12	6064.0	14	148.0	NM	669.0	47	9.5	0.2	28.9	14	2.65
ATHON GROUP	3895.0**	-12	15668.0	-4	38.0	-77	456.0	-32	1.0	3.8	12.6	21	1.58
ERGY	1596.1	92	5756.2	109	12.4	NM	111.8	397	0.8	NM	9.3	16	2.03
ESOURCES	634.1	-43	3306.6	-2	66.9	-3	240.5	9	10.6	6.2	53.9	14	2.46
OLEUM SERVICES													
OMPOSITE	10100.9	25	36413.3	28	1039.3	37	3439.0	57	10.3	9.4	17.6	25	2.02
GHES (3)	1133.4	37	3992.1	26	79.4	54	137.0	-30	7.0	6.2	5.3	48	0.82
ES (3)	415.4	22	1541.6	40	44.1	121	132.0	157	10.6	5.9	13.7	20	3.11
AMERON	514.3**	24	1806.1	30	47.3	94	140.6	119	9.2	5.9	22.5	22	2.51
OFFSHORE DRILLING	272.3	46	956.1	56	79.3	41	278.6	90	29.1	30.0	18.1	24	1.93
ARINE	319.3	45	1067.1	57	58.8	-47	315.1	75	18.4	50.1	43.3	14	1.79
ION	2385.3**	20	8818.6	19	148.4	38	454.4	51	6.2	5.4	18.6	28	1.75
INDUSTRIES (3)	302.8	39	1115.0	44	41.3	105	136.0	80	13.6	9.3	18.7	19	1.24
ILIATES	323.2**	17	1116.6	26	32.6	12	99.3	18	10.1	10.5	12.7	22	1.75
ERGER	2907.7	16	10647.6	19	372.7	46	1295.7	52	12.8	10.1	19.4	31	2.52
ERNATIONAL	425.9	26	1563.1	35	30.0	51	102.4	59	7.1	5.9	23.4	22	2.55
R (9)	280.7	52	1002.4	52	70.3	71	225.0	111	25.0	22.3	23.8	12	3.69
NTAIGNE OIL (8)	545.1	97	1703.1	124	2.4	-10	10.1	52	0.4	1.0	7.0	35	0.40
ORD ENTERRA	275.6	-3	1084.0	9	32.7	50	112.9	61	11.9	7.7	12.3	17	2.14
ALTH CARE													
Y COMPOSITE	78294.0	14	298214.6	15	6220.6	7	24084.6	-3	7.9	8.5	21.9	38	1.78
I DISTRIBUTION													
OMPOSITE	24476.0	23	92715.2	29	446.5	66	1394.1	10	1.8	1.4	11.2	37	1.18
RCE HEALTH (3)	2254.6	29	8323.6	38	14.5	23	50.1	10	0.6	0.7	169.5	29	2.06
JGS (5)	254.2	13	992.0	15	7.8	22	35.8	27	3.1	2.8	15.6	26	0.89
RUNSWIG (3)	3169.0	12	12007.4	16	21.3	17	84.8	12	0.7	0.6	13.2	28	1.67
HEALTH (6)	3130.5	11	11616.6	15	66.2	60	220.7	62	2.1	1.5	15.1	39	2.01
	3336.4	9	12738.2	16	110.8	19	37.3	-89	3.3	3.0	1.2	NM	0.14
JG STORES (11)	714.6	7	2958.3	8	10.0	7	58.0	19	1.4	1.4	10.4	20	1.49
(9)	4670.8**	34	17479.9	52	42.0	NM	156.0	NM	0.9	NM	11.7	33	1.63
	283.0	80	895.7	67	16.3	24	55.7	28	5.8	8.4	7.4	49	0.69
(6)	292.2	0	1067.9	0	2.8	NM	-4.3	NM	1.0	NM	-5.1	NM	-0.36
(0)	2885.7	94	10841.6	89	67.9	82	251.9	55	2.4	2.5	8.9	16	2.00
(4)	3485.0	14	13794.0	14	87.0	16	448.0	17	2.5	2.5	18.5	38	0.92
S & RESEARCH													
OMPOSITE	28910.6	12	108056.4	11	5077.4	17	17050.5	1	17.6	16.9	30.9	39	2.19
BORATORIES	3118.1	4	11883.5	8	566.7	11	2094.5	11	18.2	17.0	43.3	26	2.72
	311.7	-1	1149.0	-1	45.5	26	128.3	66	14.6	11.5	15.2	19	1.95
HOME PRODUCTS	3611.4	4	14196.0	1	571.8	12	2043.1	8	15.8	14.7	27.4	29	3.11
	606.7	2	2401.0	7	179.7	1	644.3	-5	29.6	30.0	30.1	23	2.35

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 12-31	PRICE-EARNING RATIO 2-6
	4TH QUARTER 1997 \$ MIL	CHANGE FROM 1996 %	12 MONTHS 1997 \$ MIL	CHANGE FROM 1996 %	4TH QUARTER 1997 \$ MIL	CHANGE FROM 1996 %	12 MONTHS 1997 \$ MIL	CHANGE FROM 1996 %	4TH QUARTER 1997 %	4TH QUARTER 1996 %		
BRISTOL-MYERS SQUIBB	4441.0	12	16701.0	11	802.0	12	3205.0	12	18.1	18.1	46.3	31
CHIRON	311.2	-1	1162.1	5	33.8	140	50.8	-10	10.9	4.5	5.8	71
GENENTECH	258.3**	21	947.6	5	41.5	456	129.0	9	16.1	3.5	6.4	64
LILLY (ELI)	2415.8	17	8517.6	16	457.5	23	-385.1	NM	18.9	18.1	-8.8	NM
MERCK †	6232.1	15	23636.9	19	1242.2	19	4614.1	19	19.9	19.3	36.0	31
PFIZER	3496.0	11	12504.0	11	558.0	11	2213.0	15	16.0	16.0	29.9	48
SCHERING-PLOUGH	1781.0	26	6778.0	20	343.0	24	1444.0	19	19.3	19.6	53.4	38
WARNER-LAMBERT	2327.4	26	8179.8	13	235.7	38	869.5	11	10.1	9.3	31.9	49
(C) HEALTH-CARE SERVICES												
GROUP COMPOSITE	13003.9	7	51445.3	9	-475.4	NM	927.1	-46	NM	1.1	4.7	45
BEVERLY ENTERPRISES	778.0	-7	3217.1	-2	-8.0	NM	58.6	13	NM	NM	5.5	25
COLUMBIA/HCA HEALTHCARE	4374.0	-9	18819.0	0	-749.0	NM	182.0	-88	NM	8.3	2.1	90
GENESIS HEALTH VENTURES (3)	302.6**	17	1143.8	44	12.8	11	49.5	16	4.2	4.5	8.1	21
HUMANA	2337.0**	29	7880.0	16	48.0	118	173.0	NM	2.1	1.2	11.9	20
MANOR CARE (7)	280.3	8	1393.5	18	25.4	11	129.0	83	9.1	8.8	17.7	18
NOVACARE (5)	398.8	70	1377.5	62	20.6	123	52.9	219	5.2	3.9	10.2	15
QUEST DIAGNOSTICS	365.4	-5	1528.7	-5	-37.4	NM	-22.3	NM	NM	NM	-4.0	NM
QUORUM HEALTH GROUP (6)	408.9	20	1557.5	27	24.4	21	92.2	22	6.0	5.9	16.2	22
TENET HEALTHCARE (7)	2429.0	15	9348.5	15	138.0	34	-18.0	NM	5.7	4.9	-0.5	NM
TRIGON HEALTHCARE	517.7	7	2063.6	7	22.5	-59	95.1	-52	4.3	11.4	9.9	12
VENCOR	812.3	22	3116.0	21	27.2	NM	135.1	181	3.4	NM	14.2	14
(D) MEDICAL PRODUCTS												
GROUP COMPOSITE	11903.6	8	45997.8	6	1172.2	8	4712.8	-4	9.8	9.9	20.7	36
BARD (C. R.)	311.3	-1	1213.5	2	23.8	-10	72.3	-22	7.6	8.4	12.6	26
BAUSCH & LOMB	473.0	9	1915.7	-1	7.4	-53	49.4	-41	1.6	3.7	5.9	50
BAXTER INTERNATIONAL	1632.0	9	6138.0	13	182.0	15	300.0	-48	11.2	10.6	12.2	53
BECTON, DICKINSON (3)	701.6	7	2856.4	3	64.3	11	306.3	3	9.2	8.9	22.2	28
GUIDANT	495.8	83	1328.2	27	66.8	75	150.0	187	13.5	14.1	31.0	68
JOHNSON & JOHNSON	5630.0	2	22629.0	5	630.0	13	3303.0	14	11.2	10.1	27.1	29
MALLINCKRODT (6)	656.2	45	2120.4	8	-4.7	NM	-276.1	NM	NM	8.6	-32.0	NM
MEDTRONIC (8)	642.1**	7	2527.6	9	143.5	12	564.2	17	22.4	21.5	29.1	45
OWENS & MINOR	804.7	7	3116.8	3	7.1	49	24.3	88	0.9	0.6	13.8	26
STRYKER	254.4	5	980.1	8	37.0	20	125.3	20	14.5	12.7	20.5	31
U. S. SURGICAL	302.5	7	1172.1	5	15.0	-53	94.1	-14	5.0	11.2	7.1	23
13 HOUSING & REAL ESTATE												
INDUSTRY COMPOSITE	14749.6	11	54856.2	8	625.7	-7	2733.9	48	4.2	5.1	20.1	18
(A) BUILDING MATERIALS												
GROUP COMPOSITE	8799.8	10	34911.3	8	414.4	-13	2078.1	46	4.7	5.9	26.8	17
AMERICAN STANDARD	1539.0	7	6008.0	4	46.0	2	120.0	NM	3.0	3.2	NM	26
JOHNS MANVILLE	402.5	-5	1647.6	6	27.0	NM	130.5	-31	6.7	0.0	19.3	14
LAFARGE	473.1	6	1806.4	10	59.2	16	182.0	29	12.5	11.4	14.8	13
OWENS CORNING	1243.0	24	4373.0	14	-102.0	NM	62.0	NM	NM	7.0	NM	24
PPG INDUSTRIES	1846.0	5	7379.0	2	159.0	5	714.0	-4	8.6	8.7	28.5	16
RPM (7)	397.8	26	1518.0	25	21.4	16	85.5	14	5.4	5.9	16.4	20
SHERWIN-WILLIAMS	1091.4	14	4881.1	18	45.1	15	260.6	14	4.1	4.1	16.7	19
TECUMSEH PRODUCTS	379.1	-3	1728.3	-3	15.3	-25	100.5	-11	4.0	5.3	10.0	11
USG	721.0	8	2874.0	11	72.0	454	148.0	887	10.0	1.9	211.4	18
VALSPAR (2)	292.6	23	1017.3	18	20.2	16	65.9	18	6.9	7.3	22.3	21
VULCAN MATERIALS	414.3	4	1678.6	7	51.1	7	209.1	11	12.3	12.0	21.1	16
(B) CONSTRUCTION & REAL ESTATE												
GROUP COMPOSITE	5949.8	14	19944.9	8	211.3	7	655.8	54	3.6	3.8	11.4	20
CENTEX (9)	983.1**	5	3788.1	4	37.4	36	129.8	39	3.8	2.9	14.2	16
FLEETWOOD ENTERPRISES (8)	769.1	3	2871.9	-1	28.1	9	94.0	14	3.7	3.4	18.9	16
HOVNANIAN ENTERPRISES (2)	315.2**	-8	784.1	-3	7.7	-38	-7.0	NM	2.5	3.6	-3.9	NM
KAUFMAN & BROAD HOME (1)	646.9	24	1876.3	5	27.9	40	58.2	NM	4.3	3.8	15.2	18
LENNAR (1)	466.1**	38	1303.1	25	8.2	-59	50.6	-2	1.8	5.8	17.7	20
M.D.C. HOLDINGS	271.8**	8	969.6	5	8.2	29	24.2	16	3.0	2.5	10.5	14
OAKWOOD HOMES (3)	254.7**	23	1117.5	14	17.8	17	84.5	22	7.0	7.3	16.8	20
PULTE	846.1**	15	2524.0	6	17.3	31	49.8	-21	2.0	3.4	6.1	20
RYLAND GROUP	499.1	14	1649.8	4	9.5	91	21.9	38	1.9	1.1	6.6	20
STARWOOD HOTELS & RESORTS TRUST	300.8	84	933.6	118	13.3	86	41.6	61	4.4	4.4	4.1	61
TOLL BROTHERS (2)	318.1**	22	971.7	28	24.6	11	67.8	26	7.7	8.5	17.6	16
WEBB (DEL) (6)	278.9**	-5	1155.3	-1	11.3	4	40.3	NM	4.0	3.7	12.7	12
14 LEISURE TIME INDUSTRIES												
INDUSTRY COMPOSITE	29208.9	4	104364.1	6	846.9	-48	5942.7	-9	2.9	5.8	11.4	36
(A) EATING PLACES												
GROUP COMPOSITE	5736.4	8	21814.8	9	445.4	-2	1791.4	-4	7.8	8.6	15.0	25
BRINKER INTERNATIONAL (6)	374.5	20	1466.2	22	13.4	15	62.4	3	3.6	3.7	11.5	20
CKE RESTAURANTS (11)	347.5	114	995.6	81	13.1	134	40.4	109	3.8	3.4	8.6	45
CRACKER BARREL OLD COUNTRY STORE (5)	312.8	21	1177.7	20	23.7	26	91.5	40	7.6	7.3	13.2	25
DARDEN RESTAURANTS (7)	745.3	0	3172.1	0	7.5	NM	-68.4	NM	1.0	NM	-6.4	NM

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 12-31	PRICE- EARNINGS RATIO 2-6	12 MONTHS' EARNINGS PER SHARE
	4TH QUARTER 1997 \$ MIL	CHANGE FROM 1996 %	12 MONTHS 1997 \$ MIL	CHANGE FROM 1996 %	4TH QUARTER 1997 \$ MIL	CHANGE FROM 1996 %	12 MONTHS 1997 \$ MIL	CHANGE FROM 1996 %	4TH QUARTER 1997 %	4TH QUARTER 1996 %			
MODMAKER (3)	343.8**	6	1092.0	3	11.7	29	38.0	56	3.4	2.8	43.2	19	0.95
OST MARRIOTT SERVICES	388.2	-1	1284.6	1	11.1	22	20.8	45	0.3	0.2	NM	23	0.57
CDONALD'S	2952.6	5	11408.8	7	410.9	0	1642.5	4	13.9	14.5	18.0	21	2.29
HONEY'S (2)	271.9	-3	1217.7	11	-36.0	NM	-35.7	NM	NM	4.1	NM	NM	-0.74
I) ENTERTAINMENT													
GROUP COMPOSITE	7051.9	1	25385.6	6	794.4	2	2183.9	29	11.3	11.2	11.4	36	2.47
RCUS CIRCUS ENTERPRISES (11) †	315.0	2	1232.4	-3	27.2	-22	104.3	-14	8.6	11.2	9.3	21	1.11
SNEY (WALT) (3)	6339.0	1	22534.0	6	755.0	1	1972.0	34	11.9	11.9	11.4	38	2.87
ARRAH'S ENTERTAINMENT	398.0	7	1619.2	2	12.1	NM	107.5	9	3.1	NM	14.6	21	1.06
J) HOTEL & MOTEL													
GROUP COMPOSITE	5215.0	16	17350.0	23	103.0	-11	585.0	27	2.0	2.6	12.2	30	1.46
LTON HOTELS	1339.0	29	5316.0	35	-5.0	NM	250.0	60	NM	0.6	7.4	30	0.95
MARRIOTT INTERNATIONAL	3876.0	12	12034.0	18	108.0	-2	335.0	9	2.8	3.2	22.5	29	2.46
K) OTHER LEISURE													
GROUP COMPOSITE	11205.5	-2	39813.9	-1	-495.9	NM	1382.4	-45	NM	2.5	8.5	51	0.89
ERICAN GREETINGS (10)	639.7	-1	2208.1	5	79.0	6	188.7	19	12.4	11.5	13.8	18	2.50
UNSWICK	931.1	16	3657.4	16	32.7	12	151.2	-19	3.5	3.6	11.7	21	1.51
ARNIVAL (1)	524.4	10	2447.5	11	155.4	35	666.1	18	29.6	24.2	19.1	25	2.23
STMAN KODAK	3779.0	-12	14538.0	-9	-744.0	NM	5.0	NM	NM	NM	0.1	NM	0.01
ARLEY-DAVIDSON	451.0	17	1774.9	15	43.4	17	174.1	21	9.6	9.7	22.1	23	1.13
ISERO	1133.4	2	3188.6	6	18.9	-81	135.0	-32	1.7	9.0	7.3	35	1.02
ATION	569.8	-2	2201.8	-3	-157.8	NM	-180.1	NM	NM	NM	-26.4	NM	-4.54
ATTEL	1613.1	13	4834.6	7	195.1	82	289.8	-22	12.1	7.5	15.8	44	0.94
USICLAND STORES	676.2	-3	1768.3	-3	65.7	NM	14.0	NM	9.7	NM	74.4	22	0.41
CLARIS INDUSTRIES	280.3	-6	1048.3	-12	18.4	9	65.4	5	6.6	5.7	41.0	12	2.44
LAROID	607.6	-8	2146.4	-6	-202.8	NM	-126.7	NM	NM	2.0	-26.2	NM	-2.81
L) MANUFACTURING													
GROUP COMPOSITE	54908.9	13	194419.4	10	2758.6	4	11445.3	6	5.0	5.5	18.2	20	2.18
M) GENERAL MANUFACTURING													
GROUP COMPOSITE	18349.7	8	69967.4	9	1129.7	20	5251.3	23	6.2	5.6	21.5	20	2.57
ROQUIP-VICKERS	522.8	3	2112.3	4	31.4	28	100.9	-2	6.0	4.8	19.8	16	3.51
ITLER MFG.	254.4	-6	924.6	6	6.7	-16	34.4	33	2.6	2.9	22.1	8	4.43
RLISLE	319.7	15	1260.6	24	16.7	27	70.7	27	5.2	4.7	20.3	21	2.28
ILTEC INDUSTRIES	359.0	20	1314.9	13	26.3	21	94.9	74	7.3	7.3	NM	17	1.42
ARNING	1085.0**	9	4129.1	12	108.5	19	439.8	28	10.0	9.1	35.2	19	1.85
IDE (9)	691.7	2	2246.7	-6	23.1	-12	16.0	68	3.3	3.9	4.7	32	0.72
RST BRANDS (6)	309.3	10	1163.1	6	13.3	-13	43.0	-37	4.3	5.5	11.2	24	1.06
RTUNE BRANDS	1186.4	3	4425.8	4	-25.8	NM	41.5	-77	NM	5.4	1.0	26	1.48
ACE (W. R.)	852.1	0	3312.8	-4	26.1	NM	248.6	16	3.1	NM	51.8	24	3.28
XCEL	254.6	20	936.9	35	12.3	440	73.6	NM	4.8	1.1	31.4	16	1.74
ELLENBRAND INDUSTRIES (1)	475.0	13	1776.0	5	46.0	18	157.0	12	9.7	9.2	17.7	24	2.28
INOIS TOOL WORKS	1348.9	4	5220.4	4	160.2	19	587.0	21	11.9	10.4	20.9	24	2.33
HNSON CONTROLS (3)	3056.3	11	11440.4	15	65.3	19	231.1	-1	2.1	2.0	13.3	21	2.53
ARK IV INDUSTRIES (10)	564.1	8	2174.5	4	27.3	NM	108.4	297	4.8	NM	14.6	13	1.66
MINNESOTA MINING & MFG.	3713.0	2	15070.0	6	366.0	-2	2121.0	40	9.9	10.4	35.8	17	5.06
WELL	914.1	21	3234.3	13	90.6	12	290.4	13	9.9	10.7	17.7	23	1.82
ARKER HANNIFIN (6)	1114.9	15	4360.3	13	71.3	36	319.9	35	6.4	5.4	20.0	16	2.85
IBBERMAID	574.3	-7	2399.7	2	31.8	60	142.5	-6	5.5	3.2	13.6	27	0.95
WER AUTOMOTIVE	433.9	262	1235.8	209	17.0	145	48.7	136	3.9	5.8	9.4	20	2.28
PPERWARE	320.1	-14	1229.3	-10	15.7	-79	82.0	-53	4.9	20.1	33.7	20	1.32
N) MACHINE & HAND TOOLS													
GROUP COMPOSITE	4450.4	10	15749.4	6	265.3	26	725.8	-10	6.0	5.2	13.0	26	1.82
ACK & DECKER	1518.4	4	4940.5	1	97.0	7	227.2	43	6.4	6.2	12.7	21	2.35
NCINNATI MILACRON	496.4	9	1896.7	10	26.8	34	80.6	22	5.4	4.4	17.8	14	2.01
NAHER	565.1	14	2051.0	13	43.2	24	154.8	21	7.7	7.0	17.8	27	2.57
NNAMETAL (6)	370.0	35	1288.5	16	9.6	-34	69.4	-4	2.6	5.3	13.1	20	2.63
NCOLN ELECTRIC	287.1	4	1159.1	5	20.2	14	85.4	15	7.0	6.5	19.5	11	3.45
IAP-ON	514.5**	21	1744.1	13	42.0	15	150.4	14	8.2	8.6	16.9	16	2.46
ANLEY WORKS	698.8	2	2669.5	0	26.5	NM	-41.9	NM	3.8	NM	-6.9	NM	-0.47
O) SPECIAL MACHINERY													
GROUP COMPOSITE	28094.1	17	92925.8	13	1269.6	-10	5000.5	-3	4.5	5.9	16.9	20	2.10
ICO	888.7	29	3224.4	39	50.0	25	170.8	32	5.6	5.8	17.3	10	2.74
PLIED MATERIALS (2)	1280.4	49	4074.3	-2	180.1	147	498.5	-17	14.1	8.5	16.9	27	1.32
HIGGS & STRATTON (6)	308.5	3	1334.1	9	10.3	-38	57.8	-31	3.3	5.6	18.7	22	2.04
ISE	1747.0**	11	6024.0	11	123.0	21	403.0	15	7.0	6.5	17.4	12	5.10
TERPILLAR	5193.0	16	18925.0	15	451.0	18	1665.0	22	8.7	8.5	35.5	12	4.37
JMMINS ENGINE	1559.0	15	5625.0	7	64.0	56	212.0	33	4.1	3.0	15.8	10	5.48
ERE (2)	3444.1**	18	12791.4	14	211.3	22	960.1	17	6.1	6.0	23.2	14	3.78
IVER	1221.1	17	4547.7	12	100.3	25	405.4	4	8.2	7.7	24.9	21	1.69

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 12-31	PRICE-EARNINGS RATIO 2-6	12 MONTH EARNINGS PER SHAR
	4TH QUARTER 1997 \$ MIL.	CHANGE FROM 1996 %	12 MONTHS 1997 \$ MIL.	CHANGE FROM 1996 %	4TH QUARTER 1997 \$ MIL.	CHANGE FROM 1996 %	12 MONTHS 1997 \$ MIL.	CHANGE FROM 1996 %	4TH QUARTER 1997 %	4TH QUARTER 1996 %			
DRESSER INDUSTRIES (2)	2100.2	15	7419.1	14	109.6	28	318.0	24	5.2	4.7	18.4	21	1.8
FMC	1072.4	-2	4259.0	8	-161.4	NM	-24.5	NM	NM	2.8	-2.6	NM	-0.6
HARNISCHFEGER INDUSTRIES (2)	810.8	13	3118.2	8	41.1	108	152.8	34	5.1	2.8	20.0	11	3.2
INGERSOLL-RAND	1932.5	11	7103.3	6	94.0	-14	380.5	6	4.9	6.3	16.7	19	2.3
LAM RESEARCH (6)	292.1	13	1060.3	-17	3.5	8	-5.4	NM	1.2	1.3	-8.5	NM	-1.7
McDERMOTT INTERNATIONAL (9)	901.7	21	3482.3	6	51.0	117	9.2	NM	5.7	3.2	-1.9	NM	-0.29
PENTAIR	523.5	23	1839.1	17	29.5	32	91.6	23	5.6	5.2	15.6	18	2.1
STEWART & STEVENSON SERVICES (11)	299.0	29	1170.8	39	3.5	-6	25.8	112	1.2	1.6	5.2	30	0.78
TIMKEN	671.1	9	2617.6	9	47.6	22	171.4	23	7.1	6.3	16.6	12	2.69
TYCO INTERNATIONAL (3)	2687.5	17	NA	NA	240.8	60	NA	NA	9.0	6.6	NA	NA	N/A
U. S. FILTER (9)	829.4	79	2884.2	118	-374.1	NM	-320.1	NM	NM	1.4	-21.3	NM	-3.42
UNOVA	332.1	5	1426.2	22	-5.6	NM	-171.4	NM	NM	4.0	-29.1	NM	-3.17
(D) TEXTILES													
GROUP COMPOSITE	4014.7	7	15776.8	7	93.9	1	467.6	-23	2.3	2.5	15.9	22	1.03
BURLINGTON INDUSTRIES (3)	481.7	1	2095.9	-2	13.2	41	62.5	47	2.7	2.0	9.7	15	1.03
COLLINS & AIKMAN	429.7	37	1629.3	43	9.0	126	-10.1	NM	2.1	1.3	NM	NM	-0.15
DEXTER	294.6	10	1147.1	4	13.3	16	56.4	16	4.5	4.3	15.1	17	2.4
MOHAWK INDUSTRIES	516.1	12	1901.4	7	19.3	54	68.0	39	3.7	2.7	16.8	20	1.30
SHAW INDUSTRIES	928.9	6	3575.8	12	-32.4	NM	29.0	-15	NM	NM	4.5	51	0.22
SPRINGS INDUSTRIES	574.9	7	2226.1	0	15.2	45	69.0	-22	2.6	2.0	8.6	16	3.34
UNIFI (6)	343.1	-18	1543.8	-6	33.0	15	123.5	23	9.6	6.9	21.1	20	1.98
WESTPOINT STEVENS	445.6	12	1657.5	10	23.1	20	69.3	19	5.2	4.8	NM	22	2.22
16 METALS & MINING													
INDUSTRY COMPOSITE	24324.3	5	97343.0	6	839.1	94	4223.1	37	3.5	1.9	12.2	16	1.82
(A) ALUMINUM													
GROUP COMPOSITE	7123.7	4	28233.4	1	269.3	82	1088.0	21	3.8	2.2	11.9	20	2.77
ALUMAX	781.1	12	2930.9	-7	47.2	147	33.7	-87	6.0	2.7	2.1	60	0.60
ALUMINUM CO. OF AMERICA	3298.6	1	13319.2	2	210.3	55	805.1	56	6.4	4.2	17.7	17	4.59
KAISER ALUMINUM	594.6	10	2373.2	8	14.2	NM	48.0	485	2.4	NM	36.3	19	0.57
MAXXAM	682.4	10	2729.1	7	14.6	NM	65.2	185	2.1	NM	136.4	7	7.14
REYNOLDS METALS	1767.0	2	6881.0	-1	-17.0	NM	136.0	31	NM	0.1	5.0	35	1.84
(B) STEEL													
GROUP COMPOSITE	11433.3	8	45119.3	6	509.4	NM	1809.1	122	4.5	NM	13.6	12	1.70
AK STEEL HOLDING	620.5	2	2440.5	6	40.4	32	150.9	3	6.5	5.0	16.3	8	2.43
ARMCO	436.4	6	1829.3	6	17.8	35	77.1	197	4.1	3.2	NM	9	0.58
BETHLEHEM STEEL	1118.4	3	4631.2	-1	41.7	NM	280.7	NM	3.7	NM	20.5	5	2.03
BIRMINGHAM STEEL (6)	267.5	27	1090.4	25	2.8	-53	12.2	868	1.0	2.8	2.6	42	0.40
CARPENTER TECHNOLOGY (6)	280.0	34	1065.0	22	18.7	37	74.0	28	6.7	6.5	16.0	12	3.68
COMMERCIAL METALS (4)	550.5**	4	2277.9	1	8.1	-12	37.5	-16	1.5	1.7	10.4	13	2.49
INLAND STEEL INDUSTRIES	1233.2	10	5046.8	10	17.7	NM	119.3	73	1.4	0.1	12.1	10	2.13
LTV	1147.0	13	4446.1	8	39.0	13	41.3	-62	3.4	3.4	2.4	31	0.37
NATIONAL STEEL	768.5	0	3139.7	6	48.7	76	213.5	296	6.3	3.6	27.3	3	4.82
NUCOR	1037.3	12	4184.5	15	76.5	-7	294.5	19	7.4	8.9	16.3	15	3.39
ROUGE INDUSTRIES	331.5	4	1341.6	3	-4.5	NM	22.4	-4	NM	NM	5.1	14	1.02
TEXAS INDUSTRIES (7)	286.3**	20	1085.3	11	23.4	31	85.8	8	8.2	7.5	17.2	13	3.98
USX-U. S. STEEL GROUP	1808.0	2	6871.0	5	152.0	20	452.0	64	8.4	7.2	26.8	7	4.88
WALTER INDUSTRIES (7)	448.1	13	1586.9	6	12.6	68	46.1	NM	2.8	1.9	14.3	22	0.88
WEIRTON STEEL	324.5	-5	1397.2	1	3.1	NM	-17.7	NM	1.0	NM	-11.9	NM	-0.42
WHX	255.4	53	642.1	-48	-10.6	NM	-173.8	NM	NM	NM	-38.5	NM	-8.83
WORTHINGTON INDUSTRIES (7)	520.3	14	2043.8	17	21.9	-3	93.3	-2	4.2	4.9	12.7	17	0.96
(C) OTHER METALS													
GROUP COMPOSITE	5767.3	2	23990.3	14	60.4	-79	1326.0	-4	1.0	5.2	11.0	17	1.52
ASARCO	603.2	7	2721.0	0	5.1	-79	143.4	4	0.9	3.7	8.5	7	3.42
COMMONWEALTH INDUSTRIES	260.2	8	1090.8	48	1.2	-79	9.1	-38	0.5	2.3	2.8	18	0.78
CYPRUS AMAX MINERALS	757.0	1	3346.0	18	-97.0	NM	69.0	-10	NM	NM	2.0	30	0.54
ENGELHARD	1013.6**	24	3630.7	14	-54.1	NM	66.5	-56	NM	5.2	7.6	39	0.46
ESSEX INTERNATIONAL	392.1	10	1701.4	28	19.3	62	84.0	124	4.9	3.3	28.6	13	2.83
FREEPORT-McMORAN COPPER & GOLD	420.7	-32	2000.9	5	48.6	-45	245.1	8	11.6	14.2	64.1	15	1.06
GENERAL CABLE	285.2	18	1134.5	9	15.3	33	53.2	36	5.4	4.7	43.5	18	2.17
HARSCO †	430.9	-5	1629.1	4	29.8	28	100.4	20	6.9	5.7	12.8	20	2.04
NEWMONT MINING	412.2	35	1572.8	42	38.6	80	68.3	-31	9.4	7.0	4.3	64	0.44
PHILIPS DODGE	865.9	-11	3914.3	3	32.0	-69	408.5	-12	3.7	10.5	16.3	10	6.63
PRECISION CASTPARTS (9)	326.4	19	1248.8	48	21.6	41	78.4	56	6.6	5.6	14.3	16	3.29
17 NONBANK FINANCIAL													
INDUSTRY COMPOSITE	118400.0	13	450133.6	13	10481.2	20	43225.7	28	8.9	8.3	16.0	19	3.35
(A) FINANCIAL SERVICES													
GROUP COMPOSITE	56439.3	17	214621.8	18	4994.1	6	21738.4	15	8.8	9.8	20.1	20	2.82
ADVANTA	285.3**	18	938.2	10	43.6	-3	71.6	-59	15.3	18.7	8.1	21	1.50
AMERICAN EXPRESS	4674.0**	9	17760.0	8	493.0	-17	1991.0	5	10.5	13.8	21.8	21	4.15
ASSOCIATES FIRST CAPITAL	2184.3	15	8278.6	17	278.0	19	1031.7	20	12.7	12.4	16.5	24	2.94
BEAR STEARNS (6)	1993.1	28	7090.7	29	160.2	-9	650.2	13	8.0	11.3	21.0	10	4.57



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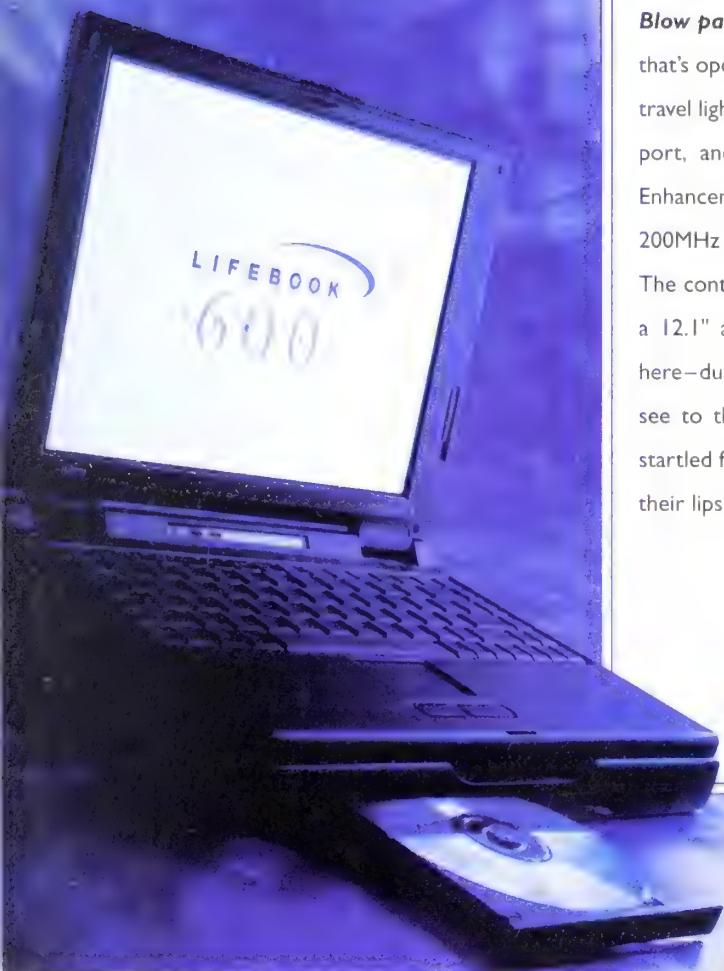
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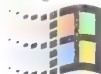


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CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 12-31	PRICE EARNINGS RATIO 2-6
	4TH QUARTER 1997 \$ MIL	CHANGE FROM 1-97 %	12 MONTHS 1997 \$ MIL	CHANGE FROM 1996 %	4TH QUARTER 1997 \$ MIL	CHANGE FROM 1996 %	12 MONTHS 1997 \$ MIL	CHANGE FROM 1996 %	4TH QUARTER 1997 %	4TH QUARTER 1996 %		
BENEFICIAL	704.8	7	2955.7	7	-12.8	NM	253.7	-10	NM	3.5	14.7	18
CAPITAL ONE FINANCIAL	519.6	25	1787.1	26	58.2	45	189.4	22	11.2	9.7	21.2	23
CIT GROUP	534.5	9	2072.5	10	71.0	13	310.1	19	13.3	12.8	12.7	15
COUNTRYWIDE CREDIT INDUSTRIES (10)	729.0	31	2007.9	30	80.2	22	328.2	33	11.0	11.8	17.0	16
DONALDSON, LUFKIN & JENRETTE	1329.4	40	4640.5	33	101.4	39	408.3	40	7.6	7.7	22.5	13
EDWARDS (A. G.) (10)	527.3	30	1932.9	17	72.4	42	255.6	23	13.7	12.6	18.2	16
EQUIFAX	367.0	11	1366.1	12	38.6	-19	185.5	21	10.5	14.3	51.6	25
FANNIE MAE	7238.0**	11	27776.9	11	805.6	13	3068.6	11	11.1	10.9	24.5	22
FINOVA GROUP	269.7	26	975.0	20	38.8	28	139.1	19	14.4	14.2	14.2	21
FIRST AMERICAN FINANCIAL	552.4**	30	1887.5	18	22.8	93	64.7	21	4.1	2.8	16.6	14
FRANKLIN RESOURCES (3)	632.4**	45	2358.0	46	130.5	36	468.3	39	20.6	22.0	25.3	13
FREDDIE MAC	3795.0	17	14399.0	19	372.0	16	1395.0	11	9.8	9.9	19.4	25
GREEN TREE FINANCIAL	468.5	7	1707.7	34	-17.3	NM	301.4	63	NM	NM	22.9	11
HOUSEHOLD INTERNATIONAL	1451.4	9	5453.1	8	217.6	33	686.6	27	15.0	12.3	15.6	20
LEHMAN BROTHERS HOLDINGS (1)	1023.0**	-4	3873.0	12	185.0	46	647.0	56	18.1	11.9	15.1	12
MARSH & McLENNAN	1625.5	44	6008.6	36	-50.0	NM	399.4	-13	NM	8.7	12.0	31
MERRILL LYNCH	8123.0	23	31731.0	27	466.0	5	1906.0	18	5.7	6.7	25.3	14
MORGAN STANLEY, DEAN WITTER, DISCOVER (1)	3732.0**	22	14833.0	24	810.0	79	2586.0	32	21.7	14.8	21.0	15
PAINWEBBER GROUP	1745.0**	19	6656.9	17	108.7	19	415.4	14	6.2	6.2	22.0	13
RAYMOND JAMES FINANCIAL (3)	252.3	30	951.9	25	22.7	32	104.5	48	9.0	8.8	24.7	11
SCHWAB (CHARLES)	768.4	28	2845.3	25	63.1	6	270.3	16	8.2	9.9	25.1	38
SLM HOLDING	884.7	-3	3784.7	5	133.7	22	511.2	24	15.1	12.1	75.8	16
TRAVELERS GROUP	9765.0	14	37608.6	16	376.7	-35	3103.7	5	3.9	6.8	17.0	21
UNITED ASSET MANAGEMENT	264.8	12	941.6	8	-75.4	NM	-4.1	NM	NM	14.6	-0.9	NM
(B) INSURANCE												
GROUP COMPOSITE	57690.1	9	219093.1	10	4990.6	29	19985.4	44	8.7	7.4	13.5	17
AETNA	4792.9**	7	18540.2	22	273.9	NM	901.1	339	5.7	NM	8.1	14
AFLAC	1744.9	-3	6983.5	-1	96.0	-28	585.0	48	5.5	7.5	20.9	15
ALLSTATE	6313.0	4	24949.0	3	871.0	46	3105.0	50	13.8	9.8	20.3	13
AMERICAN BANKERS INSURANCE GROUP	402.3	9	1621.4	6	30.0	15	114.9	22	7.5	7.1	15.8	23
AMERICAN GENERAL	2324.0**	6	8927.0	2	230.0	142	542.0	-17	9.9	4.3	7.5	26
AMERICAN INTERNATIONAL GROUP	7189.7**	6	27916.5	8	884.6	15	3332.3	15	12.3	11.3	13.9	24
AON	1520.8	42	5750.6	48	112.9	144	298.8	2	7.4	4.3	9.8	34
CIGNA	5492.0**	12	20038.0	6	240.0	-22	1086.0	3	4.4	6.3	13.6	12
CINCINNATI FINANCIAL	482.4	5	1942.4	7	72.5	15	299.4	34	15.0	13.7	6.3	24
EQUITABLE	2327.5	3	9666.1	16	70.2	NM	648.2	215	3.0	NM	12.2	18
FREMONT GENERAL	306.1	57	974.3	22	30.2	29	108.3	24	9.9	12.0	14.4	16
GENERAL RE	2031.2**	-10	8246.6	-1	246.7	-1	967.7	8	12.1	11.0	11.7	18
HARTFORD FINANCIAL SERVICES GROUP	3739.0	12	13305.0	7	255.0	24	1332.0	NM	6.8	6.2	22.9	8
HARTFORD LIFE	1544.0**	20	4699.0	2	87.0	55	306.0	NM	5.6	4.3	14.3	20
JEFFERSON-PILOT	673.1	23	2578.3	21	86.8	16	394.4	34	12.9	13.7	14.2	15
LIBERTY FINANCIAL	319.0	3	1247.0	9	31.6	9	129.5	29	9.9	9.4	10.7	12
LINCOLN NATIONAL	1305.3**	4	4898.5	3	-137.7	NM	22.2	-94	NM	7.5	0.5	NM
OHIO CASUALTY	350.0	-7	1437.4	-2	40.8	-25	130.3	34	11.7	14.5	9.9	12
OLD REPUBLIC INTERNATIONAL	515.1	11	1962.8	9	75.4	21	298.1	27	14.6	13.5	14.1	13
PROGRESSIVE	1319.5**	41	4608.2	32	105.3	15	400.1	28	8.0	9.8	19.4	21
PROVIDENT	989.0**	74	3538.1	54	75.8	73	247.3	70	7.7	7.7	8.1	19
RELiance GROUP HOLDINGS	939.9	17	3442.6	11	41.7	17	174.5	262	4.4	4.4	19.5	10
SAFECO	1542.9**	52	4770.3	17	79.5	-25	430.0	-2	5.2	10.4	9.4	16
ST. PAUL	1544.3	-1	6219.3	8	187.0	15	773.2	39	12.1	10.4	17.3	10
SUNAMERICA (3) †	341.2**	47	1224.4	38	123.6	54	422.3	46	36.2	34.5	16.4	21
TIG HOLDINGS	445.0**	-1	1756.0	-4	-63.0	NM	52.0	-34	NM	8.6	4.1	26
TORCHMARK	589.9	7	2319.4	5	95.3	12	347.6	6	16.2	15.3	16.9	16
TRANSAMERICA	1499.0	11	5726.5	8	189.2	66	532.0	6	12.6	8.5	17.6	14
TRAVELERS PROPERTY CASUALTY	2541.9	6	9910.9	21	360.4	38	1236.4	216	14.2	11.0	17.0	13
UICI	300.5	53	955.8	31	22.7	20	86.5	25	7.5	9.6	16.1	17
UNITRIN †	374.9	-2	1530.1	0	46.0	16	117.9	-11	12.3	10.4	7.9	21
UNUM	1030.7	0	4004.1	-1	76.2	59	370.3	56	7.4	4.7	15.8	19
USF&G	859.0**	-5	3404.0	3	54.0	-47	194.0	-26	6.3	11.3	10.2	15
(C) SAVINGS & LOAN												
GROUP COMPOSITE	4270.7	7	16418.5	5	496.5	251	1502.0	63	11.6	3.5	11.4	24
AHMANSON (H. F.)	907.1	-6	3732.9	-1	99.5	9	413.8	185	11.0	9.5	15.9	17
GOLDEN STATE BANCORP (6)	311.2	8	1218.5	8	28.9	25	104.6	148	9.3	8.0	8.7	23
GOLDEN WEST FINANCIAL	771.6	13	2913.8	10	93.5	23	354.1	-4	12.1	11.1	13.1	14
GREENPOINT FINANCIAL	258.3	4	1029.0	0	36.8	8	147.6	11	14.2	13.7	11.6	19
WASHINGTON MUTUAL	2022.5	11	7524.4	7	237.9	NM	481.8	109	11.8	NM	8.9	37

18 OFFICE EQUIPMENT & COMPUTERS

INDUSTRY COMPOSITE	108629.1	10	386038.2	12	7301.2	12	25710.5	28	6.7	6.6	19.7	36
(A) BUSINESS MACHINES & SERVICES												
GROUP COMPOSITE	6875.5	21	23899.5	18	331.6	49	1056.8	11	4.8	3.9	20.4	27
COMPUCOM SYSTEMS	525.2	-9	1949.8	-2	12.9	73	35.2	16	2.5	1.3	19.0	11
DELUXE	496.1	-1	1919.4	-3	33.3	NM	44.7	-32	6.7	NM	7.4	63
DIEBOLD	341.3	16	1226.9	19	35.0	24	122.5	26	10.3	9.6	19.2	30
MICROAGE (2)	1321.9	22	4446.3	20	7.4	17	25.0	77	0.6	0.6	10.3	9

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CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 12-31	PRICE- EARNINGS RATIO 2-6
	4TH QUARTER 1997 \$ MIL	CHANGE FROM 1996 %	12 MONTHS 1997 \$ MIL	CHANGE FROM 1996 %	4TH QUARTER 1997 \$ MIL	CHANGE FROM 1996 %	12 MONTHS 1997 \$ MIL	CHANGE FROM 1996 %	4TH QUARTER 1997 %	4TH QUARTER 1996 %		
MILLER (HERMAN) (7)	415.1	10	1592.9	16	29.6	66	97.9	57	7.1	4.7	37.2	29
PITNEY BOWES	1120.3	6	4100.5	6	147.2	15	526.0	12	13.1	12.1	28.1	25
REYNOLDS & REYNOLDS (3)	369.7	18	1441.1	22	23.7	-7	67.5	-41	6.4	8.1	15.8	31
STANDARD REGISTER	261.9	7	965.7	2	18.7	7	66.9	6	7.1	7.1	13.7	15
TECH DATA (11)	2021.5	63	6256.9	49	23.7	41	81.1	68	1.2	1.4	15.4	24
(B) COMPUTERS & PERIPHERALS												
GROUP COMPOSITE	73670.9	8	259323.5	8	3747.1	-18	14206.8	22	5.1	6.7	19.0	26
APPLE COMPUTER (3)	1578.0	-26	6530.0	-26	47.0	NM	-878.0	NM	3.0	NM	-80.3	NM
COMPAQ COMPUTER	7323.0	23	24584.0	23	667.0	37	1855.0	41	9.1	8.2	19.7	29
DATA GENERAL (3)	365.3	5	1550.0	15	3.5	-66	49.0	45	1.0	3.0	9.3	16
DELL COMPUTER (11)	3188.0	58	11002.0	60	247.0	66	847.0	105	7.7	7.4	70.2	47
DIGITAL EQUIPMENT (6)	3324.5	-1	13062.2	-4	74.8	135	274.8	NM	2.3	1.0	7.0	38
EMC	873.4	33	2937.9	29	166.2	34	538.5	39	19.0	18.9	24.6	33
GATEWAY 2000	1976.8	27	6293.7	25	92.9	5	109.8	-56	4.7	5.7	11.8	58
HEWLETT-PACKARD (2)	11789.0	16	42895.0	12	806.0	24	3119.0	21	6.8	6.4	19.3	21
INTERNATIONAL BUSINESS MACHINES	23723.0	3	78508.0	3	2093.0	3	6093.0	12	8.8	8.7	31.1	16
IOMEGA	546.8	38	1740.0	43	36.1	77	115.4	101	6.6	5.1	25.2	24
LEXMARK INTERNATIONAL GROUP	735.5	7	2493.5	5	57.0	26	163.0	28	7.8	6.6	32.6	18
MICRON ELECTRONICS (4)	558.9	33	2093.7	20	1.1	-96	63.5	20	0.2	5.9	17.4	20
NCR	1992.0	-2	6589.0	-5	36.0	414	7.0	NM	1.8	0.3	0.5	NM
QUANTUM (9)	1519.9	3	6083.4	22	-32.2	NM	255.8	NM	NM	3.5	23.0	11
SEAGATE TECHNOLOGY (6)	1673.3	-30	8047.9	-6	-183.2	NM	-107.3	NM	NM	8.9	-3.3	NM
SEQUENT COMPUTER SYSTEMS	258.5	41	833.9	40	19.1	660	38.7	398	7.4	1.4	6.7	21
SILICON GRAPHICS (6)	850.8	3	3690.4	14	-31.5	NM	25.9	NM	NM	NM	1.4	NM
STORAGE TECHNOLOGY	663.9	7	2144.7	5	83.7	23	231.8	36	12.6	10.9	16.0	16
SUN MICROSYSTEMS (6)	2450.2	18	9206.6	18	149.4	-16	718.6	27	6.1	8.6	23.7	26
UNISYS	1898.6	5	6636.0	4	-965.7	NM	-853.6	NM	NM	3.1	NM	NM
WESTERN DIGITAL (6)	969.6	-13	4235.8	19	-145.2	NM	88.0	-41	NM	5.7	16.3	22
XEROX	5412.0	7	18166.0	5	525.0	23	1452.0	20	9.7	8.4	29.6	22
(C) COMPUTER SOFTWARE & SERVICES												
GROUP COMPOSITE	28082.8	16	102815.1	19	3222.5	89	10446.9	39	11.5	7.0	20.9	49
ADAPTEC (9)	254.2	1	1068.8	24	36.1	-13	205.3	102	14.2	16.5	23.6	13
AFFILIATED COMPUTER SERVICES (6)	285.2	27	880.4	34	5.6	-52	39.9	11	2.0	5.2	8.8	31
AMERICA ONLINE (1)	592.0	45	2039.5	45	20.8	NM	23.4	NM	3.5	NM	9.9	NM
ASCEND COMMUNICATIONS	292.5	2	1167.4	31	47.6	-26	-124.4	NM	16.3	22.4	-12.8	NM
AUTOMATIC DATA PROCESSING (6)	1148.0**	15	4392.4	12	147.4	16	545.4	13	12.8	12.8	20.2	34
BAY NETWORKS (6)	644.9	25	2302.1	10	59.5	NM	-17.0	NM	9.2	NM	-1.2	NM
CABLETRON SYSTEMS (10)	331.8	-8	1446.4	9	19.9	-71	196.6	27	6.0	18.7	15.9	10
CADENCE DESIGN SYSTEMS	283.0	33	915.9	24	60.9	NM	181.7	526	21.5	NM	25.0	36
CERIDIAN	282.5	12	1074.8	14	76.1	107	35.4	-74	26.9	14.6	12.9	NM
CISCO SYSTEMS (5)	1868.7	30	6874.1	45	336.5	86	1204.3	32	18.0	12.6	25.1	58
COMDISCO (3)	744.0**	18	2930.0	16	36.0	20	137.0	17	4.8	4.7	16.6	25
COMPUSA (6)	1456.7	22	5069.9	19	34.1	44	113.1	55	2.3	2.0	24.7	27
COMPUTER ASSOCIATES INTERNATIONAL (9)	1239.0	18	4456.9	13	339.9	NM	1103.6	274	27.4	NM	58.2	29
COMPUTER SCIENCES (9)	1664.1	17	6266.9	17	69.1	20	256.0	96	4.2	4.0	14.1	27
COMPUWARE (9)	309.6	45	1034.1	38	54.5	69	163.2	113	17.6	15.1	26.7	48
ELECTRONIC ARTS (9)	391.2	35	848.6	34	58.6	51	67.6	40	15.0	13.3	12.9	32
ELECTRONIC DATA SYSTEMS	4228.2	6	15235.6	6	283.4	4	730.6	69	6.7	6.8	14.5	28
FIRST DATA	1379.7**	2	5234.5	6	54.9	-76	356.7	44	4.0	16.6	10.8	39
FISERV	269.5	16	974.4	11	24.2	19	90.8	14	9.0	8.8	13.3	31
GALILEO INTERNATIONAL	313.6	10	1351.5	10	22.3	54	157.5	35	7.1	5.1	24.2	23
GTECH HOLDINGS (10)	264.8	14	983.0	16	23.9	25	86.5	22	9.0	8.2	21.9	14
INACOM	1069.1	16	3896.3	26	10.3	64	29.5	57	1.0	0.7	9.1	13
INTERGRAPH	300.9	2	1124.3	3	-20.7	NM	-70.2	NM	NM	NM	-19.0	NM
MICROSOFT (6)	3585.0	34	13098.0	39	1133.0	53	3895.0	57	31.6	27.7	34.0	54
NOVELL (2)	269.3	-30	1007.3	-27	7.2	-88	-78.3	NM	2.7	15.4	-5.0	NM
ORACLE (7)	1613.7	23	6303.2	30	187.3	4	725.0	3	11.6	13.7	27.2	37
PEOPLESOFT	260.6	76	815.7	81	39.5	NM	108.3	202	15.1	1.2	25.9	92
SABRE GROUP HOLDINGS	440.0	17	1783.1	10	18.0	-18	200.0	7	4.1	5.8	26.5	20
3COM (7)	1220.3	-14	4437.8	13	15.1	-87	45.1	-88	1.2	8.1	8.0	57
VANSTAR (8)	741.7	36	2498.1	23	9.3	-16	25.0	21	1.3	2.0	13.6	23
WANG LABORATORIES (6)	338.9	-1	1304.4	17	12.4	-18	14.3	-60	3.7	4.4	0.0	83
19 PAPER & FOREST PRODUCTS												
INDUSTRY COMPOSITE	25226.8	2	99542.3	0	-530.8	NM	1174.7	-67	NM	2.5	3.2	91
(A) FOREST PRODUCTS												
GROUP COMPOSITE	4103.2	2	16474.7	-1	-99.4	NM	-100.5	NM	NM	NM	1.5	NM
GEORGIA-PACIFIC GROUP	3221.0	2	12968.0	1	-104.0	NM	-86.0	NM	NM	NM	NA	NM
LOUISIANA-PACIFIC	595.1	3	2402.5	-3	-21.3	NM	-101.8	NM	NM	NM	-7.9	NM
RAYONIER	287.1	-5	1104.2	-6	25.9	NM	87.3	NM	9.0	NM	14.0	14
(B) PAPER												
GROUP COMPOSITE	21123.6	2	83067.6	0	-431.4	NM	1275.2	-66	NM	3.5	3.5	76
BOISE CASCADE	1444.9	14	5493.8	8	7.2	238	-30.4	NM	0.5	0.2	-4.3	NM
BOWATER	401.0	8	1484.5	-14	30.1	62	53.7	-74	7.5	5.0	4.5	42
CHAMPION INTERNATIONAL	1482.9	4	5735.5	-2	-520.2	NM	-548.5	NM	NM	0.7	-17.1	NM

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T H I N K C O M P U T I N G

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 12-31	PRICE- EARNINGS RATIO 2-6
	4TH QUARTER 1997 \$ MIL	CHANGE FROM 1996 %	12 MONTHS 1997 \$ MIL	CHANGE FROM 1996 %	4TH QUARTER 1997 \$ MIL	CHANGE FROM 1996 %	12 MONTHS 1997 \$ MIL	CHANGE FROM 1996 %	4TH QUARTER 1997 %	4TH QUARTER 1996 %		
CONSOLIDATED PAPERS	509.7	40	1679.3	9	35.8	-4	118.0	-34	7.0	10.2	9.0	22
FORT JAMES	1761.5	-1	7259.0	-6	-211.1	NM	104.5	-68	NM	5.6	26.4	NM
INTERNATIONAL PAPER	5100.0	-1	20115.0	0	132.0	NM	151.0	NM	2.6	NM	-1.7	NM
KIMBERLY-CLARK	3089.4	-7	12546.6	5	-147.0	NM	884.0	-37	NM	10.4	20.7	35
MEAD	1243.8	8	5077.4	8	31.8	9	150.1	-21	2.6	2.5	6.6	24
POTLATCH	379.8	0	1568.9	1	5.7	-70	36.1	-41	1.5	5.0	3.8	36
UNION CAMP	1187.1	10	4476.8	12	33.3	NM	81.1	-5	2.8	NM	3.9	51
WESTVACO (2)	783.1	1	2982.3	-2	51.7	-7	162.7	-23	6.6	7.1	7.1	21
WEYERHAEUSER	2870.0	4	11210.0	1	98.0	0	342.0	-26	3.4	3.5	7.4	30
WILLAMETTE INDUSTRIES	870.4	4	3438.7	0	21.2	-22	73.0	-62	2.4	3.3	3.7	54
20 PUBLISHING & BROADCASTING												
INDUSTRY COMPOSITE	14241.0	10	50879.4	15	241.6	-81	2040.2	-9	1.7	9.9	4.9	94
BELO (A. H.)	364.8	64	1248.4	51	24.1	-21	83.0	-5	6.6	13.7	6.3	38
CBS	1471.0	45	5363.0	29	-10.0	NM	-131.0	NM	NM	NM	-2.2	NM
DOW JONES	689.5	3	2561.9	3	-889.3	NM	-802.1	NM	NM	8.9	-47.7	NM
GANNETT	1318.8	10	4729.5	7	230.4	-20	712.7	14	17.5	24.2	21.7	25
KNIGHT-RIDDER	815.6	29	2876.8	21	86.6	6	396.5	114	10.6	12.9	23.5	14
McGRAW-HILL	900.8	8	3534.1	15	67.0	-78	290.7	41	7.4	37.1	20.6	25
NEW YORK TIMES	768.4	7	2866.4	9	79.3	50	262.3	210	10.3	7.3	16.2	25
PRIMEDIA	397.6	5	1487.6	8	-0.9	NM	-157.4	NM	NM	15.1	NM	NM
READER'S DIGEST ASSOCIATION (6)	812.5	-7	2694.3	-9	54.3	-35	12.7	-75	6.7	9.6	3.6	NM
SCHOLASTIC (7)	354.8	4	986.9	-1	26.0	-32	-11.3	NM	7.3	11.2	-3.6	NM
SCRIPPS (E. W.)	359.6	11	1242.0	11	50.5	-12	157.7	21	14.1	17.8	15.3	26
TIME WARNER	3836.0	4	13294.0	32	247.0	319	301.0	NM	6.4	1.6	-0.2	NM
TIMES MIRROR	918.4	5	3318.5	-2	72.2	-8	250.3	21	7.9	9.0	197.7	26
TRIBUNE	710.8	17	2719.8	13	113.4	39	393.6	39	16.0	13.5	26.1	22
WASHINGTON POST	522.4	4	1956.3	6	91.0	39	281.6	28	17.4	13.0	20.4	19
21 SERVICE INDUSTRIES												
INDUSTRY COMPOSITE	41740.9	18	153741.3	23	698.5	13	3438.1	24	1.7	1.8	10.9	32
(A) CONSTRUCTION & ENGINEERING												
GROUP COMPOSITE	8436.3	7	31961.0	17	280.0	19	610.8	77	3.3	3.0	8.4	26
BROWNING-FERRIS INDUSTRIES (3)	1344.7	-10	5632.6	-4	86.8	21	298.6	NM	6.5	4.8	11.2	22
EG&G	386.8	5	1460.8	2	20.6	44	30.6	-44	5.3	3.9	9.7	38
FLUOR (2)	4002.7	20	14298.5	30	88.0	12	146.2	-45	2.2	2.4	8.4	24
FOSTER WHEELER	985.3	-20	4011.0	0	2.3	-77	-10.5	NM	0.2	0.8	-1.7	NM
JACOBS ENGINEERING GROUP (3)	506.4	17	1853.3	5	12.8	18	48.8	17	2.5	2.5	15.1	15
McDERMOTT (J. RAY) (9)	452.7	43	1704.9	25	51.0	31	31.5	53	11.3	12.3	0.6	81
MORRISON KNUDSEN (1)	439.3**	5	1677.3	154	9.4	67	32.0	NM	2.1	1.3	9.6	18
STONE & WEBSTER	318.5	3	1322.5	14	9.1	82	33.5	NM	2.8	1.6	9.7	15
(B) INDUSTRIAL DISTRIBUTION												
GROUP COMPOSITE	21322.8	25	77808.2	30	263.1	NM	1094.0	4	1.2	NM	7.1	37
AIRGAS (9)	367.8	24	1368.5	26	11.8	8	35.6	-20	3.2	3.7	9.0	31
ALLEGIANCE	1136.6	4	4350.8	-1	24.9	NM	90.9	NM	2.2	NM	9.6	22
APPLIED INDUSTRIAL TECHNOLOGIES (6)	368.6	34	1316.4	15	7.7	29	27.9	11	2.1	2.2	10.2	20
AVNET (6)	1460.7	10	5636.6	6	52.1	14	189.0	2	3.6	3.4	12.6	14
BOISE CASCADE OFFICE PRODUCTS	718.5	29	2596.7	31	17.7	23	56.9	3	2.5	2.6	11.5	21
BRIGHTPOINT	373.2	76	1035.6	76	9.3	105	25.5	131	2.5	2.1	12.8	37
CELLSTAR (1)	406.5	39	1482.8	56	17.3	110	53.6	NM	4.3	2.8	33.3	15
CRANE	515.9	11	2036.8	10	29.5	18	112.8	22	5.7	5.4	21.2	18
ENRON	5872.0	45	20273.0	53	169.0	28	105.0	-82	2.9	3.3	1.8	NM
GRAINGER (W. W.)	1032.9	14	4136.6	17	63.2	12	231.8	11	6.1	6.3	17.5	22
HUGHES SUPPLY (11)	486.3	20	1734.5	19	13.1	26	40.6	34	2.7	2.6	12.4	15
KAMAN	272.4**	14	1044.8	10	61.1	757	70.5	199	22.4	3.0	38.4	6
MARSHALL INDUSTRIES (7)	351.2	23	1304.6	14	9.4	1	40.2	-5	2.7	3.3	10.3	13
NATIONAL-OILWELL	299.9	49	1005.6	32	21.1	NM	51.3	408	7.0	NM	20.6	32
NGC	3764.5	27	13378.4	84	-149.5	NM	-87.7	NM	NM	1.6	-8.0	NM
PHYSICIAN SALES & SERVICE (9)	257.2	30	866.9	24	5.2	18	11.0	-15	2.0	2.2	4.7	67
PIONEER-STANDARD ELECTRONICS (9)	424.1	10	1643.2	10	8.4	50	30.1	26	2.0	1.5	12.7	12
RYERSON TULL	683.0	20	2789.4	17	15.8	49	62.8	-1	2.3	1.9	15.3	9
UNISOURCE WORLDWIDE (3)	1869.1	8	7249.0	3	-100.6	NM	-62.1	NM	NM	1.2	-6.3	NM
UNITED STATIONERS	662.2	10	2558.1	11	-23.6	NM	8.2	-74	NM	1.6	3.0	NM
(C) PRINTING & ADVERTISING												
GROUP COMPOSITE	2556.7	5	9057.2	4	89.5	-33	336.1	804	3.5	5.5	13.7	23
ADVO (3)	262.1	3	1023.5	4	8.4	36	29.0	177	3.2	2.4	NM	19
BANTA	352.6	22	1202.5	11	15.1	1	43.3	-15	4.3	5.2	10.6	19
DONNELLEY (R. R.) & SONS	1402.0	0	4850.0	-4	45.2	-53	206.5	NM	3.2	6.9	12.5	26
WORLD COLOR PRESS	540.0	12	1981.2	21	20.9	30	57.2	21	3.9	3.3	12.7	19
(D) OTHER SERVICES												
GROUP COMPOSITE	9425.1	19	34914.9	20	65.9	-85	1397.2	4	0.7	5.5	18.0	34
ABM INDUSTRIES (2)	358.1**	24	1252.5	15	9.1	31	27.2	-16	2.5	2.4	14.2	26
ACCUSTAFF	675.1	43	2424.8	50	28.0	NM	102.0	227	4.1	NM	12.5	29
BORG-WARNER SECURITY	396.2	-11	1548.0	-10	6.2	0	19.0	37	1.6	1.4	29.2	22

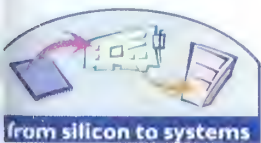
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COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 12-31	PRICE- EARNINGS RATIO 2-6
	4TH QUARTER 1997 \$ MIL.	CHANGE FROM 1996 %	12 MONTHS 1997 \$ MIL.	CHANGE FROM 1996 %	4TH QUARTER 1997 \$ MIL.	CHANGE FROM 1996 %	12 MONTHS 1997 \$ MIL.	CHANGE FROM 1996 %	4TH QUARTER 1997 %	3TH QUARTER 1996 %		
CASEY'S GENERAL STORES (8)	318.8*	11	1179.0	14	10.8	21	30.6	10	3.4	3.1	12.1	24
CENDANT	1424.7	29	5314.7	36	-345.3	NM	55.4	-87	NM	14.3	21.7	NM
HANDLEMAN	315.3	-9	1133.3	-4	8.3	22	8.6	NM	2.6	2.0	3.0	25
INTERIM SERVICES	412.9	35	1608.3	40	12.0	20	42.5	85	2.9	3.3	9.0	24
KELLY SERVICES	1011.2	14	3852.9	17	23.5	11	80.8	11	2.3	2.4	14.9	16
NORRELL	368.2	32	1300.0	28	-0.4	NM	24.5	-3	NM	2.6	11.8	23
NOVACARE EMPLOYEE SERVICES (6)	302.8	NA	952.8	NA	1.1	NA	2.7	NA	0.4	NA	NA	NA
OLSTEN	1084.5**	17	4113.0	22	23.3	41	93.0	70	2.1	1.8	11.2	13
PITTSBURGH BRINK'S GROUP	301.2	24	1101.4	21	21.2	18	73.6	23	7.0	7.4	19.4	21
ROBERT HALF INTERNATIONAL	368.5	42	1302.9	45	26.9	52	93.7	53	7.3	6.8	23.8	44
SERVICE CORP. INTERNATIONAL	644.0	6	2468.4	8	91.9	25	374.6	41	14.3	12.1	14.3	25
SERVICEMASTER	1043.5	19	3961.5	15	130.8	103	329.1	34	12.5	7.4	62.7	17
VOLT INFORMATION SCIENCES (2)	400.3	28	1401.5	-1	18.5	75	40.0	76	4.6	3.4	22.5	19

22 TELECOMMUNICATIONS

INDUSTRY COMPOSITE	69658.0	7	261114.5	7	6051.0	-11	21452.6	-17	8.7	10.4	18.1	26
(A) EQUIPMENT & SERVICES												
GROUP COMPOSITE	34288.2	7	126531.1	8	2124.5	-25	7030.2	-28	6.2	8.8	12.4	39
ADC TELECOMMUNICATIONS (2)	335.2	31	1164.5	41	36.8	31	108.8	24	11.0	11.0	14.5	25
AIRTOUCH COMMUNICATIONS †	941.0	31	3594.0	60	111.0	316	448.0	125	11.8	3.7	9.0	56
AT&T	12828.0	0	51319.0	2	1323.0	6	4472.0	-20	10.3	9.7	20.7	23
CENTURY TELEPHONE ENTERPRISES †	273.6	41	901.5	20	98.2	226	256.0	98	35.9	15.5	20.6	14
DSC COMMUNICATIONS	445.1	14	1575.5	14	-37.6	NM	48.9	NM	NM	4.5	4.0	48
EXCEL COMMUNICATIONS	467.1	30	1454.4	8	-17.5	NM	87.9	-39	NM	8.7	11.7	22
LUCENT TECHNOLOGIES (3)	8724.0	10	27146.0	14	792.0	-8	474.0	-56	9.1	10.8	14.0	NM
MCI COMMUNICATIONS	5108.0	7	19653.0	6	-391.0	NM	2.0	NM	NM	6.4	0.0	NM
PAGING NETWORK	256.1	14	961.0	17	-42.7	NM	-141.4	NM	NM	NM	NM	NM
SCIENTIFIC-ATLANTA (6)	294.5	4	1213.4	11	14.8	8	67.4	220	5.0	4.9	12.0	18
SPRINT	3849.0	8	14873.9	7	194.9	-21	952.5	-20	5.1	6.9	10.5	27
TELEPHONE & DATA SYSTEMS †	412.3	29	1471.5	25	-35.0	NM	-9.5	NM	NM	3.8	-0.6	NM
TELLABS	354.3	30	1203.5	39	77.5	31	263.7	124	21.9	21.8	28.3	37
(B) TELEPHONE COMPANIES												
GROUP COMPOSITE	35369.8	7	134583.4	6	3926.5	-1	14422.4	-11	11.1	11.9	23.3	20
ALLTEL	848.6	5	3263.6	2	110.2	14	507.9	74	13.0	12.0	23.0	16
AMERITECH	4147.0	7	15998.0	7	610.0	7	2296.0	8	14.7	14.7	27.6	20
BELL ATLANTIC	7695.7	4	30193.9	4	940.0	28	2454.9	-22	12.2	10.0	19.6	29
BELLSOUTH	5600.0	11	20561.0	8	738.0	17	3270.0	14	13.2	12.5	21.6	18
CINCINNATI BELL	461.0	7	1756.8	12	30.4	-41	193.6	5	6.6	11.9	33.4	23
FRONTIER	593.2	2	2352.9	-9	-14.4	NM	54.6	-75	NM	1.7	5.3	81
GTE	6347.0	10	23260.0	9	702.0	-10	2794.0	0	11.1	13.6	36.2	19
SBC COMMUNICATIONS	6633.0	7	24856.0	6	588.0	-18	1474.0	-54	8.9	11.6	15.5	49
SOUTHERN NEW ENGLAND TELECOMMS.	508.3**	7	2022.3	4	52.3	18	197.5	2	9.9	9.0	34.9	22
U S WEST COMMUNICATIONS GROUP	2516.0	-3	10319.0	2	170.0	-45	1180.0	-3	6.8	12.0	28.1	20

23 TRANSPORTATION

INDUSTRY COMPOSITE	46805.5	10	183678.1	10	1846.7	11	9955.0	30	3.9	3.9	16.7	16
(A) AIRLINES												
GROUP COMPOSITE	20590.5	8	83277.7	7	1213.9	86	5366.6	61	5.9	3.4	33.7	10
ALASKA AIR GROUP	422.8	18	1739.4	9	15.1	NM	72.4	91	3.6	NM	15.2	14
AMERICA WEST HOLDINGS	472.9	8	1875.0	8	20.1	66	75.0	680	4.2	2.7	11.0	14
AMR	4636.0	7	18570.0	5	208.0	-44	985.0	-11	4.5	8.6	16.4	12
CONTINENTAL AIRLINES	1839.0	18	7213.0	13	73.0	55	389.0	20	4.0	3.0	47.5	10
DELTA AIR LINES (6)	3433.0	7	13946.0	8	190.0	52	934.0	275	5.5	3.9	28.6	10
NORTHWEST AIRLINES	2491.3	6	10225.8	4	114.7	341	605.8	13	4.6	1.1	NM	11
SOUTHWEST AIRLINES	975.6	17	3816.8	12	80.6	186	317.8	53	8.3	3.4	16.7	20
UAL	4235.0	7	17378.0	6	33.0	65	963.0	61	0.8	0.5	37.6	9
US AIRWAYS GROUP	2085.0	2	8513.8	5	479.4	NM	1024.7	289	23.0	1.3	366.6	6
(B) RAILROADS												
GROUP COMPOSITE	8831.3	0	35394.3	9	402.8	-58	2907.9	-14	4.6	10.8	10.5	20
BURLINGTON NORTHERN SANTA FE	2187.0	5	8413.0	3	217.0	-11	885.0	0	9.9	11.7	13.0	16
CSX	1062.0	1	10621.0	1	215.0	-15	799.0	-7	7.9	9.4	13.9	16
KANSAS CITY SOUTHERN INDUSTRIES †	294.3**	33	1058.3	25	-116.2	NM	-14.1	NM	NM	14.7	-1.8	NM
NORFOLK SOUTHERN	1062.0**	4	4223.0	3	239.0	21	806.0	7	22.5	19.3	13.9	15
UNION PACIFIC	2561.0	-9	11079.0	26	-152.0	NM	432.0	41	NM	8.2	5.1	36
(C) TRANSPORTATION SERVICES												
GROUP COMPOSITE	13560.5	23	50648.6	19	159.9	136	1400.5	51	1.2	0.6	10.8	27
AIRBORNE FREIGHT	755.5	16	2912.4	17	30.8	187	120.1	338	4.1	1.6	18.8	15
AVIS RENT A CAR	520.5	16	2046.2	10	0.5	-78	27.5	31	0.1	0.5	6.1	40
CNF TRANSPORTATION	1194.2	21	4266.8	17	29.3	50	120.9	51	2.5	2.0	19.5	22
FDX (7)	3299.2	16	12571.4	16	107.0	3	445.8	45	3.2	3.6	13.9	17

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 12-31	PRICE- EARNINGS RATIO 2-6	12 MONTHS' EARNINGS PER SHARE
	4TH QUARTER 1997 \$ MIL.	CHANGE FROM 1996 %	12 MONTHS 1997 \$ MIL.	CHANGE FROM 1996 %	4TH QUARTER 1997 \$ MIL.	CHANGE FROM 1996 %	12 MONTHS 1997 \$ MIL.	CHANGE FROM 1996 %	4TH QUARTER 1997 %	4TH QUARTER 1996 %			
(7)	343.6	12	1250.1	16	6.9	-26	-6.0	NM	2.0	3.0	-2.5	NM	-0.17
	441.7**	9	1701.9	20	-140.3	NM	-50.9	NM	NM	4.7	-6.9	NM	-2.55
	934.5	5	3891.3	6	34.6	-4	201.6	27	3.7	4.0	18.1	23	1.86
GROUP	271.6	5	1064.5	41	2.8	16	9.5	35	1.0	0.9	8.8	18	1.46
PORT NEWS SHIPBUILDING	512.0	18	1788.0	-4	16.0	433	44.0	-20	3.1	0.7	16.6	22	1.23
ON BURLINGTON GROUP	448.6	11	1664.8	12	13.2	25	32.3	-4	2.9	2.6	10.0	16	1.62
LIC INDUSTRIES	2928.2	83	10305.6	69	-28.8	NM	200.2	NM	NM	NM	6.5	54	0.46
SYSTEM	1268.4	5	4893.9	-1	49.2	NM	160.2	NM	3.9	NM	13.5	17	2.05
Y INDUSTRIES (9)	642.4	11	2291.7	0	38.8	76	95.3	-14	6.0	3.8	11.1	21	2.19
TRUCKING & SHIPPING													
P COMPOSITE	3823.2	7	14357.5	8	70.1	NM	280.0	NM	1.8	NM	11.0	18	1.38
NDER & BALDWIN	335.3**	1	1275.4	3	20.0	16	81.4	25	6.0	5.2	11.4	16	1.80
SAS BEST	400.1	0	1643.7	2	4.9	NM	21.0	NM	1.2	NM	11.5	12	0.84
LIDATED FREIGHTWAYS	571.6	3	2299.1	7	-1.6	NM	20.4	NM	NM	NM	8.8	18	0.89
(J. B.) TRANSPORT SERVICES	415.2	9	1554.3	5	7.0	31	11.4	-49	1.7	1.4	3.3	81	0.31
WAY EXPRESS	828.7	6	2670.9	13	13.2	24	36.9	69	1.6	1.4	15.3	13	1.80
IGHTWAYS	435.2	27	1565.2	18	14.7	85	56.6	80	3.4	2.3	14.9	16	2.19
W	837.1	7	3348.9	9	11.9	NM	52.4	NM	1.4	NM	11.8	15	1.83
UTILITIES & POWER													
STRY COMPOSITE	73349.1	27	262635.6	20	3018.7	-21	17988.6	-8	4.1	6.6	10.1	18	1.87
ELECTRIC, WATER & COGENERATION													
P COMPOSITE	61394.7	28	223012.6	20	2339.4	-26	15754.1	-10	3.8	6.6	9.9	18	1.86
HENY ENERGY	531.0	87	1411.0	69	56.0	56	188.0	50	10.5	12.7	13.0	39	1.11
IN	616.6	7	2369.5	2	79.5	56	290.6	33	12.9	8.9	12.6	14	2.30
CAN ELECTRIC POWER	731.9	-2	3326.5	0	49.6	107	399.1	7	6.8	3.2	13.3	13	2.82
	1703.1	18	6161.3	5	127.7	-10	638.2	1	7.5	9.8	13.4	15	3.28
IG ENERGY	272.0	20	1102.0	12	-5.1	NM	85.0	21	NM	1.4	9.2	15	1.42
ORE GAS & ELECTRIC	812.6	11	3307.6	5	24.3	NM	282.8	-9	3.0	NM	8.9	18	1.72
N EDISON	407.3	4	1776.2	7	8.3	-1	144.6	2	2.0	2.2	12.1	14	2.71
ERGY	628.0**	229	2270.9	294	-52.9	NM	51.8	-44	NM	11.1	34.5	33	0.77
INA POWER & LIGHT	735.1	6	3024.1	1	83.9	3	388.3	-1	11.4	11.7	13.6	15	2.66
AL & SOUTH WEST	1330.0	8	5268.0	2	26.0	-55	331.0	5	2.0	4.7	9.1	17	1.55
IP	382.7	129	976.5	59	-17.9	NM	12.9	-59	NM	1.9	2.8	64	0.71
Y	1102.2	26	4352.8	34	113.5	54	375.2	5	10.3	8.4	14.5	15	2.28
ENERGY	1436.0	21	4787.0	10	70.0	37	294.0	10	4.9	4.3	14.6	16	2.58
ONWEALTH ENERGY SYSTEM	281.9	7	1042.1	3	17.7	32	49.9	-16	6.3	5.1	11.6	16	2.27
LIDATED EDISON	1720.1	5	7121.3	2	143.6	20	712.8	3	8.4	7.4	11.7	15	2.95
RVA POWER & LIGHT	366.0	26	1423.5	21	22.5	4	105.7	-9	6.2	7.5	10.6	13	1.66
ION RESOURCES	1887.0	58	7436.3	54	108.7	46	434.7	-14	5.8	6.2	7.9	19	2.15
	367.0	6	1332.9	1	35.4	8	182.3	5	9.7	9.5	14.6	15	1.20
	298.5	1	1219.2	-1	48.6	20	199.1	11	16.3	13.6	13.3	13	2.57
ERGY	973.9	10	3764.5	3	132.4	64	429.0	32	13.6	9.1	11.9	13	2.88
ENERGY	4589.7	22	16308.9	33	184.6	-4	974.4	-9	4.0	5.1	11.9	22	2.51
I INTERNATIONAL	2329.4	6	9235.0	8	149.3	16	742.5	-3	6.4	5.9	12.1	16	1.73
	626.5	14	2217.0	11	82.9	47	258.2	9	13.2	10.3	16.3	12	2.20
ENERGY	973.3	59	2823.9	14	77.4	1	333.7	1	8.0	12.5	11.8	15	1.94
A PROGRESS	848.3	9	3315.6	5	-51.2	NM	55.7	-78	NM	6.0	2.9	69	0.56
UP	1477.7	3	6369.0	6	94.7	4	637.6	6	6.4	6.3	12.7	16	3.57
	1032.4	10	4143.4	4	95.8	28	347.5	14	9.3	8.0	10.6	14	2.77
IAN ELECTRIC INDUSTRIES	377.4	2	1464.0	4	24.4	8	92.7	9	6.5	6.1	10.8	15	2.75
ON INDUSTRIES	2772.3	206	6873.4	68	-3.9	NM	423.4	-1	NM	4.6	8.4	16	1.66
ENERGY	1099.5	0	4263.8	19	26.9	116	102.4	-6	2.5	1.1	11.8	16	1.47
SLAND LIGHTING	779.6	5	3147.7	0	56.8	-11	334.0	6	7.3	8.6	11.3	13	2.33
ERICAN ENERGY HOLDINGS	521.6	-3	1922.3	3	30.9	-7	141.6	-8	5.9	6.2	10.1	15	1.42
NA POWER	291.9	-1	1023.6	5	51.4	10	128.6	8	17.6	15.8	12.7	13	2.28
ENTURY ENERGIES	883.9	9	3342.5	8	88.9	41	273.2	-4	10.1	7.8	12.6	18	2.50
WGLAND ELECTRIC SYSTEM	658.2	10	2502.6	6	60.1	22	227.4	5	9.1	8.3	12.7	12	3.39
ORK STATE ELECTRIC & GAS	558.7	9	2130.0	3	48.0	1	184.6	4	8.3	8.9	9.8	14	2.57
INDUSTRIES	807.1	39	2586.5	30	58.1	8	199.5	8	7.2	9.2	15.1	17	3.06
EAST UTILITIES	979.0	5	3834.8	1	-29.8	NM	-105.4	NM	NM	NM	-6.4	NM	-1.05
ERN STATES POWER	699.5	-1	2733.8	3	65.4	-18	237.3	-14	9.4	11.2	9.5	17	3.21
WESTERN PUBLIC SERVICE	283.1	102	918.1	167	8.9	21	26.3	13	3.1	5.2	14.3	17	1.31
ERGY	373.3	20	1472.3	6	12.2	67	132.6	-1	3.3	2.3	13.2	16	3.23
ORP	2005.5	91	6278.0	65	0.1	NM	225.4	-48	0.0	10.7	5.0	36	0.68
ENERGY	1144.0	13	4617.9	8	-57.0	NM	336.8	-35	NM	11.7	6.7	14	1.44
	4888.6	81	15399.9	60	102.2	-31	749.1	-1	2.1	5.5	7.9	17	1.75
LE WEST CAPITAL	443.8	10	1995.0	10	22.0	NM	248.7	9	4.9	NM	11.6	15	2.76
AC ELECTRIC POWER	390.4	-6	1863.5	-7	-27.3	NM	181.8	-23	NM	2.7	8.5	18	1.38
ESOURCES	799.2	8	3048.7	5	79.3	-1	319.3	-11	9.9	10.8	10.6	12	1.80
SERVICE CO. OF NEW MEXICO	311.7	34	1135.3	29	16.2	28	81.0	12	5.2	5.4	10.0	12	1.92

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS				RETURN ON COMMON EQUITY	PERF. IN COMMON STOCK
	1997	CHANGE FROM 1996	1997	CHANGE FROM 1996	1997	CHANGE FROM 1996	1997	CHANGE FROM 1996	1997	CHANGE FROM 1996	1997	CHANGE FROM 1996		
	\$ MIL.	%	\$ MIL.	%	\$ MIL.	%	\$ MIL.	%	%	%	%	%	12-31	2-6
PUBLIC SERVICE ENTERPRISE GROUP	1744.5	11	4870.0	8	155.0	18	574.0	-3	8.9	8.4	10.8	13		
ROCHESTER GAS & ELECTRIC	277.0	-1	1036.6	-2	14.0	-37	95.4	-2	5.2	8.1	11.1	14		
SCANA	388.0	6	1523.0	1	61.9	57	230.7	5	16.0	10.8	12.5	14		
SOUTHERN	3307.0	36	12681.0	22	206.0	30	1226.5	16	6.2	6.5	10.1	17		
TECO ENERGY	456.5	1	1862.3	3	42.7	-15	212.0	-3	9.4	11.4	14.7	16		
UNICOM	1655.0	1	7083.0	2	-536.2	NM	-178.8	NM	NM	6.7	-2.8	NM		
UTILICORP UNITED	3164.1	7	8926.3	106	31.0	11	134.1	27	1.0	1.8	11.3	14		
WASHINGTON WATER POWER	481.1	73	1300.0	39	28.0	64	104.8	35	-4.8	5.1	14.7	17		
WISCONSIN ENERGY	470.4	-1	1780.6	1	2.6	-95	61.9	-72	0.5	11.9	3.2	52		
(B) GAS, OIL & TRANSMISSION														
GROUP COMPOSITE	11954.5	22	39623.1	25	679.3	1	2234.5	11	5.7	6.8	11.8	19		
AGL RESOURCES	200.5	8	1310.3	3	28.2	-8	80.4	3	7.0	8.1	11.7	16		
AQUILA GAS PIPELINE	278.0	5	1013.9	27	4.7	-51	25.2	-22	1.7	3.6	11.5	12		
COLUMBIA ENERGY GROUP	1720.2	54	5053.6	51	75.6	11	273.3	23	-4.4	6.1	15.3	15		
EL PASO NATURAL GAS	1577.0	47	5638.0	87	57.0	135	211.0	455	3.6	2.3	9.8	20		
K N ENERGY	782.7	65	2145.1	49	28.5	20	77.5	21	3.6	5.0	13.7	21		
KEYSPAN ENERGY (3)	461.9	1	1483.4	0	56.5	26	126.5	3	12.5	10.0	12.5	14		
MCN ENERGY GROUP	103.4	16	2207.9	11	50.2	20	142.3	26	7.1	6.9	12.7	19		
NATIONAL FUEL GAS (3)	371.0	2	1273.3	1	36.8	-5	112.9	2	9.9	10.6	12.4	16		
NICOR	618.7	-1	1390.6	8	39.3	13	127.9	6	6.8	8.3	11.8	16		
ONEOK	314.2	26	1227.3	-1	12.5	3	59.6	5	4.0	4.9	5.3	17		
PACIFIC ENTERPRISES	743.0	-4	2738.0	1	42.0	-16	191.0	-9	5.7	6.4	13.0	16		
PEOPLES ENERGY	383.2	-1	1272.4	0	35.5	-5	96.5	-8	9.2	9.7	13.5	14		
SONAT	1263.6	31	4174.6	37	59.9	-11	175.9	-13	4.7	7.0	11.0	21		
UGI	471.2	-11	1583.6	-5	25.5	-11	51.8	0	5.4	5.4	13.0	20		
WASHINGTON GAS LIGHT (3)	367.5	7	1078.3	4	38.1	2	82.7	3	10.4	10.8	13.8	15		
WICOR	277.0	-1	1021.0	1	17.4	13	49.5	6	6.3	5.2	13.0	17		
WILLIAMS	1266.6	32	4409.6	25	71.5	-33	350.5	-3	5.6	11.1	10.1	28		

ALPHABETICAL LIST OF COMPANIES

The number following each company name identifies the Scoreboard category under which it is listed

A	Alcoa 16a	Alcoa 16a	Alcoa 16a	Alcoa 16a	Alcoa 16a	Alcoa 16a	Alcoa 16a	Alcoa 16a	Alcoa 16a	Alcoa 16a	Alcoa 16a	Alcoa 16a	Alcoa 16a	Alcoa 16a
B	Banque Paribas 10c	Banque Paribas 10c	Banque Paribas 10c	Banque Paribas 10c	Banque Paribas 10c	Banque Paribas 10c	Banque Paribas 10c	Banque Paribas 10c	Banque Paribas 10c	Banque Paribas 10c	Banque Paribas 10c	Banque Paribas 10c	Banque Paribas 10c	Banque Paribas 10c
C	Centex 14c	Centex 14c	Centex 14c	Centex 14c	Centex 14c	Centex 14c	Centex 14c	Centex 14c	Centex 14c	Centex 14c	Centex 14c	Centex 14c	Centex 14c	Centex 14c
D	Dana 2b	Dana 2b	Dana 2b	Dana 2b	Dana 2b	Dana 2b	Dana 2b	Dana 2b	Dana 2b	Dana 2b	Dana 2b	Dana 2b	Dana 2b	Dana 2b
E	Edison International 24a	Edison International 24a	Edison International 24a	Edison International 24a	Edison International 24a	Edison International 24a	Edison International 24a	Edison International 24a	Edison International 24a	Edison International 24a	Edison International 24a	Edison International 24a	Edison International 24a	Edison International 24a
F	Federal Mogul 2b	Federal Mogul 2b	Federal Mogul 2b	Federal Mogul 2b	Federal Mogul 2b	Federal Mogul 2b	Federal Mogul 2b	Federal Mogul 2b	Federal Mogul 2b	Federal Mogul 2b	Federal Mogul 2b	Federal Mogul 2b	Federal Mogul 2b	Federal Mogul 2b
G	General Electric 18c	General Electric 18c	General Electric 18c	General Electric 18c	General Electric 18c	General Electric 18c	General Electric 18c	General Electric 18c	General Electric 18c	General Electric 18c	General Electric 18c	General Electric 18c	General Electric 18c	General Electric 18c
H	Hess 15c	Hess 15c	Hess 15c	Hess 15c	Hess 15c	Hess 15c	Hess 15c	Hess 15c	Hess 15c	Hess 15c	Hess 15c	Hess 15c	Hess 15c	Hess 15c
I	IBM 11a	IBM 11a	IBM 11a	IBM 11a	IBM 11a	IBM 11a	IBM 11a	IBM 11a	IBM 11a	IBM 11a	IBM 11a	IBM 11a	IBM 11a	IBM 11a
J	Jacobs 14c	Jacobs 14c	Jacobs 14c	Jacobs 14c	Jacobs 14c	Jacobs 14c	Jacobs 14c	Jacobs 14c	Jacobs 14c	Jacobs 14c	Jacobs 14c	Jacobs 14c	Jacobs 14c	Jacobs 14c
K	Kaiser Aluminum 18c	Kaiser Aluminum 18c	Kaiser Aluminum 18c	Kaiser Aluminum 18c	Kaiser Aluminum 18c	Kaiser Aluminum 18c	Kaiser Aluminum 18c	Kaiser Aluminum 18c	Kaiser Aluminum 18c	Kaiser Aluminum 18c	Kaiser Aluminum 18c	Kaiser Aluminum 18c	Kaiser Aluminum 18c	Kaiser Aluminum 18c
L	Laboratory Corp. 18c	Laboratory Corp. 18c	Laboratory Corp. 18c	Laboratory Corp. 18c	Laboratory Corp. 18c	Laboratory Corp. 18c	Laboratory Corp. 18c	Laboratory Corp. 18c	Laboratory Corp. 18c	Laboratory Corp. 18c	Laboratory Corp. 18c	Laboratory Corp. 18c	Laboratory Corp. 18c	Laboratory Corp. 18c
M	Marathon Petroleum 18c	Marathon Petroleum 18c	Marathon Petroleum 18c	Marathon Petroleum 18c	Marathon Petroleum 18c	Marathon Petroleum 18c	Marathon Petroleum 18c	Marathon Petroleum 18c	Marathon Petroleum 18c	Marathon Petroleum 18c	Marathon Petroleum 18c	Marathon Petroleum 18c	Marathon Petroleum 18c	Marathon Petroleum 18c
N	National Instruments 18c	National Instruments 18c	National Instruments 18c	National Instruments 18c	National Instruments 18c	National Instruments 18c	National Instruments 18c	National Instruments 18c	National Instruments 18c	National Instruments 18c	National Instruments 18c	National Instruments 18c	National Instruments 18c	National Instruments 18c
O	Occidental Petroleum 18c	Occidental Petroleum 18c	Occidental Petroleum 18c	Occidental Petroleum 18c	Occidental Petroleum 18c	Occidental Petroleum 18c	Occidental Petroleum 18c	Occidental Petroleum 18c	Occidental Petroleum 18c	Occidental Petroleum 18c	Occidental Petroleum 18c	Occidental Petroleum 18c	Occidental Petroleum 18c	Occidental Petroleum 18c
P	Pfizer 18c	Pfizer 18c	Pfizer 18c	Pfizer 18c	Pfizer 18c	Pfizer 18c	Pfizer 18c	Pfizer 18c	Pfizer 18c	Pfizer 18c	Pfizer 18c	Pfizer 18c	Pfizer 18c	Pfizer 18c
Q	Qualcomm 18c	Qualcomm 18c	Qualcomm 18c	Qualcomm 18c	Qualcomm 18c	Qualcomm 18c	Qualcomm 18c	Qualcomm 18c	Qualcomm 18c	Qualcomm 18c	Qualcomm 18c	Qualcomm 18c	Qualcomm 18c	Qualcomm 18c
R	Ralph Lauren 18c	Ralph Lauren 18c	Ralph Lauren 18c	Ralph Lauren 18c	Ralph Lauren 18c	Ralph Lauren 18c	Ralph Lauren 18c	Ralph Lauren 18c	Ralph Lauren 18c	Ralph Lauren 18c	Ralph Lauren 18c	Ralph Lauren 18c	Ralph Lauren 18c	Ralph Lauren 18c
S	Schlumberger 18c	Schlumberger 18c	Schlumberger 18c	Schlumberger 18c	Schlumberger 18c	Schlumberger 18c	Schlumberger 18c	Schlumberger 18c	Schlumberger 18c	Schlumberger 18c	Schlumberger 18c	Schlumberger 18c	Schlumberger 18c	Schlumberger 18c
T	Texas Instruments 18c	Texas Instruments 18c	Texas Instruments 18c	Texas Instruments 18c	Texas Instruments 18c	Texas Instruments 18c	Texas Instruments 18c	Texas Instruments 18c	Texas Instruments 18c	Texas Instruments 18c	Texas Instruments 18c	Texas Instruments 18c	Texas Instruments 18c	Texas Instruments 18c
U	Union Pacific 18c	Union Pacific 18c	Union Pacific 18c	Union Pacific 18c	Union Pacific 18c	Union Pacific 18c	Union Pacific 18c	Union Pacific 18c	Union Pacific 18c	Union Pacific 18c	Union Pacific 18c	Union Pacific 18c	Union Pacific 18c	Union Pacific 18c
V	Vanguard 18c	Vanguard 18c	Vanguard 18c	Vanguard 18c	Vanguard 18c	Vanguard 18c	Vanguard 18c	Vanguard 18c	Vanguard 18c	Vanguard 18c	Vanguard 18c	Vanguard 18c	Vanguard 18c	Vanguard 18c
W	Wal-Mart Stores 18c	Wal-Mart Stores 18c	Wal-Mart Stores 18c	Wal-Mart Stores 18c	Wal-Mart Stores 18c	Wal-Mart Stores 18c	Wal-Mart Stores 18c	Wal-Mart Stores 18c	Wal-Mart Stores 18c	Wal-Mart Stores 18c	Wal-Mart Stores 18c	Wal-Mart Stores 18c	Wal-Mart Stores 18c	Wal-Mart Stores 18c
X	Xerox 18c	Xerox 18c	Xerox 18c	Xerox 18c	Xerox 18c	Xerox 18c	Xerox 18c	Xerox 18c	Xerox 18c	Xerox 18c	Xerox 18c	Xerox 18c	Xerox 18c	Xerox 18c
Y	Yale 18c	Yale 18c	Yale 18c	Yale 18c	Yale 18c	Yale 18c	Yale 18c	Yale 18c	Yale 18c	Yale 18c	Yale 18c	Yale 18c	Yale 18c	Yale 18c
Z	Zynga 18c	Zynga 18c	Zynga 18c	Zynga 18c	Zynga 18c	Zynga 18c	Zynga 18c	Zynga 18c	Zynga 18c	Zynga 18c	Zynga 18c	Zynga 18c	Zynga 18c	Zynga 18c



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CORPORATE SCOREBOARD

ALPHABETICAL LIST OF COMPANIES

The number following each company name identifies the Scoreboard category under which it is listed

Fortune Brands 15a
Foster Wheeler 21a
FPL Group 24a
Franklin Resources 17a
Freddie Mac 17a
Freeport-McMoRan 16c
Fremont General 17b
Fritz 23c
Frontier 22b
Fuller (H.B.) 4
Furniture Brands 6b

G
Galileo Intl 18c
Gannett 20
Gap 8
Gateway 2000 18b
GATX 23c
GenCorp 2b
Genentech 12b
General Cable 16c
General Dynamics 1
General Electric 5
General Mills 10b
General Motors 2a
General Nutrition 10c
General Re 17b
General Signal 9a
Genesis Health 12c
Geon 4
Georgia-Pacific Group 19a
Grant Food 10c
Gillette 6d
Global DirectMail 8
Global Marine 11b
Golden State Bancorp 17c
Golden West 17c
Good Guys 6b
Goodyear Tire & Rubber 2c
GPU 24a
Grace (W.R.) 15a
Grainger (W.W.) 21b
Grand Union 10c
Great A&P 10c
Great Lakes Chemical 4
Green Tree Financial 17a
GreenPoint Financial 17c
GTE 22b
Gtech Holdings 18c
Guidant 12d
Hawthorne Aerospace 1

H
Halliburton 11b
Handleman 21d
Hanna (M.A.) 4
Hannaford Brothers 10c
Harcourt General 5
Harley-Davidson 14d
Hartman International 6b
Harsco 16c
Harsco 9b
Harsco 16c
Hartford Financial Services 17b
Hartford Life 17b
Hasbro 14d
Hawaiian Electric 24a
Hayes Lemmerz Intl 2b
Heilig-Meyers 6b
Heinz (H.J.) 10b
Hercules 4
Hershey Foods 10b
Hertz 23c
Hewlett-Packard 18b
Hill 15a
Hillenbrand 15a
Hills Stores 14c
Hilton Hotels 14c
Home Depot 8
HomeBase 8
Honeywell 9c
Hormel Foods 10b
Host Marriott Services 14a
Household Intl 17a
Houston Industries 24a

Hovnanian Ents. 13b
Howmet International 1
Hub Group 23c
Hubbell 9a
Hughes Electronics 9b
Hughes Supply 21b
Humana 12c
Hunt (J.B.) 23d
Huntington Bancshares 3b

I
IBM 18b
IBP 10b
IKON Office Solutions 5
Illinois Tool Works 15a
Imation 14d
IMC Global 4
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Xerox 18b
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EDITED BY AMY DUNKIN

DOES YOUR WILL STILL HAVE WHAT IT TAKES?

For most people, estate planning is a "one of those days" task. That's understandable considering it is time consuming, complicated, and involves lots of tax law. Besides, it forces you to confront an unpleasant inevitability, the last and most serious taxable event in your lifelong relationship with the Internal Revenue Service: Death.

But while you're stalling, events in the here-and-now are making estate planning more important than ever. The Taxpayer Relief Act of 1997 made sweeping changes in the laws governing estate and gift taxes. For example, the new rules hike the amount you can pass on to heirs free from federal inheritance tax. This year promises more skirmishing as President Clinton's desire to squeeze revenues out of some popular planning devices collides with a GOP push to cut the estate tax (table). Throw in some recent IRS rulings, and lawyers and financial advisers agree that now's the time to give your estate plan a checkup.

Start with the basics. Estate planning is a struggle to ensure that your assets go to the recipients of your choice while leaving as little as possible to the heir you didn't choose—the IRS. For most couples, the two main tax

shields are the unified credit, which excludes the first \$625,000 in an estate's property from federal tax for deaths in 1998, and the marital deduction, which lets unlimited assets pass to a spouse tax-free. A couple's

wills are usually drafted so the assets of the first spouse to die are split by a formula. Children or other heirs get as much as can be passed tax-free under the unified credit, while the surviving spouse gets the rest. Thus, a man who dies in 1998 with \$1 million in assets would leave \$625,000 to his children and \$1,375,000 to his wife.

But the 1997 law phased out the unified credit, which had excluded \$600,000, on a sliding scale. By 2006, it will exclude an estate's first \$1 million of assets from tax. So you



ESTATE PLANNING "Everybody who owns a business will have to take a look at" one valuable new special exclusion

ke sure your will takes
stage of the increase. "If
ee a fixed dollar amount,
a red flag," says Mark
on, an Atlanta-based
er at KPMG Peat Mar-
But couples whose net
is \$600,000 to \$1.2 mil-
ould be careful. If their
use the rising credit to
mine how assets are

If the home constitutes a
large share of the estate,
joint ownership means that
ultimately less of the estate
will be sheltered. The new
regs offer an escape: A sur-
viving wife, say, can "dis-
claim" her late husband's
share of joint property. That
share can then be sheltered
by the husband's unified cred-

property pass on without
probate, are popular in states
with community property
and burdensome probate
rules. Now, they may catch
on elsewhere.

The law isn't kind to all
estate-planning vehicles. It
cracks down on charitable-
remainder trusts, which let
a donor enjoy the income

from property that
eventually will be
passed on to a char-
ity. One big appeal
is that CRTs let the
donor collect income
from stocks or other
property that has
appreciated in value
without paying cap-
ital-gains taxes.

The trouble is,
tax planners were
selling clients on
CRTs that produced
plenty of tax sav-
ings and lifetime in-
come but not much
of a charitable gift.
The new law says
trusts won't qualify
for tax deductions
unless the design-
ated charity ends
up with at least
10% of the trust's
initial value. That
rule essentially bars
donors who are
younger than 45—
and even some old-
er donors—from
setting up new
CRTs, says Evelyn
Capassakis of ac-
countant Coopers &
Lybrand. Owners of

existing CRTs must also be
careful: If they add funds to
their trusts, the plans will
become subject to the new
standard and may lose their
favored status.

Small business was a ma-
jor force pushing estate-tax
cuts in last year's budget bat-
tle. But even six months af-
ter the law passed, it's un-
clear whether the main break
aimed at smaller firms—an
extra exclusion that lets a
family-owned business pro-
tect up to \$1.3 million in as-
sets from estate taxes—is a
boon or a bust. The extra ex-

clusion can be worth a lot: A
\$2 million estate could save
almost \$304,000 in taxes. But
to use the exclusion, it has
to clear high hurdles. A busi-
ness owner's estate can't
qualify unless the business'
value makes up at least half
of the estate, as calculated
under a complex new formu-
la. That could rule out many
older business owners who
have diversified or built up
liquid assets in preparation
for retirement.

LONG HAUL. Even if an es-
tate qualifies, heirs have a
tough decision to make: Un-
less a family member or, in
some cases, a longtime em-
ployee runs the business for
the next 10 years, the IRS
will reclaim the tax break,
with interest, from the heirs.
"Let's say the daughter
agrees to run Dad's busi-
ness—but she quits after five
years," says attorney Schnei-
der. "The widow is left with
a tax bill that could be more
than the business is worth."

The choice of whether to
claim the special exclusion is
left to the business owner's
executor. But owners should
decide whether they want to
pursue the option now and
structure their succession to
meet the rules. "Everybody
who owns a business will
have to look at it," says Len
Mertz, a cattle rancher and
CPA in San Angelo, Tex. "But
darned few of them are going
to get to use it."

Whatever its flaws, the
small-business exclusion
"places a marker of Congress'
intention to relieve family
businesses of the death tax,"
says James Wickett, a tax
specialist for the National
Federation of Independent
Business. Indeed, 1997 may
have just been the opening
skirmish in a series of annual
tug of wars over the estate
tax. President Clinton, for one,
is trying to crack down on es-
tate plans that his Treasury
Dept. sees as abusive. The
Administration's budget tar-
gets family limited partner-
ships, which parents use to
mark down the value of as-
sets passed on as gifts or be-

How The 1997 Tax Law Affects Your Estate...

► The amount of estate or gifts free from tax rose to \$625,000 this year and will hit \$1 million by 2006. Be sure that your will automatically adjusts the amount of assets you leave to heirs other than your spouse.

► If you own a small business or farm, you'll need to study a new break exempting up to \$1.3 million from estate tax. But qualifying for it may be tough.

► New rules crack down on charitable-remainder trusts. Don't contribute to an existing trust or set one up unless you plan to leave a lot of the assets to charity.

...And What May Be In Store For 1998

► The Clinton Administration wants to bar the discounts that parents can currently claim on property other than an active business passed to heirs through family limited partnerships. It wants to treat funds put into life-insurance trusts as taxable gifts. And it would prevent you from claiming a deep discount on the value of your home if you give it to your children but continue to live in it.

► Republicans are pushing bills to cut or eliminate "death taxes." They're likely to fight Clinton's proposals, aided by the housing and insurance industries.

DATA TREASURY DEPT., BUSINESS WEEK

the first spouse to die
leave too much to chil-
dren and not enough to sup-
port the spouse. These cou-
ples might want to place a
limit on the first
spouse's bequest to children,
if that means passing
up some tax savings.

Middle-class couples get an
equal break from new
regulations. Many of them
have been accidentally un-
wittingly their estate plans
involving property—espe-
cially homes—in joint owner-
ship. That's convenient for
couples but bad for heirs.

it. "Lawyers who've been
hammering on clients not to
keep joint property can
breathe a sigh of relief," says
Pam Schneider, partner at
Philadelphia law firm Drinker,
Biddle, & Reath.

The '97 law also gives a
boost to revocable trusts,
which some attorneys say
are better than wills for es-
tate planning. The bill re-
moves the stricter IRS limits
on deducting charitable gifts
made through such trusts,
putting them on a par with
gifts granted under a will.
Revocable trusts, which let

ILL GROOVY TER ALL THESE YEARS

important is the
of your car? If
gn turns you on,
swagen's New

e is the ultimate. Like
original Bug, the 1998

is a study
metry. Its

AUTOS

ed fenders, curved sil-
te, and oversize oval
mps and taillights are
lly different from any-
else on the road. At
\$16,500 for a typically
ed Bug, vw should
no problem meeting its
arget of 50,000 annual
Dealers already are in-
ed with orders for the
hich is made in Mexico
oes on sale in late

R POWER. Like its
able predecessor, the
Bug wears its quirky
ality well. What other
mes equipped with a
ical bud vase on the
oard? In the Bug, it

This is a cuddly car
to conjure up dreamy
ies of the flower power
1960s. Its message:
ven still be groovy and
wn with house pay-
kids, and a 9-
job. But
need
than

once you're on the road.
While the car turned heads
during a recent test-drive
around Atlanta, I found the
New Beetle adequate but
hardly spectacular.

The Bug's interior delights
and disappoints. The instru-

ment panel
sports a single
round pod with a huge
speedometer flanked by a
tiny, hard-to-read fuel gauge
and tachometer. The top of
the dash is a deep, flat ex-
panse of black plastic, making
the windshield seem as far
away as in a minivan, while
the brightly colored interior
windowsills appear prone to
chips and scratches.

The seats are firm and
comfortable, and provide
plenty of leg- and headroom
for the driver and front-seat
passenger. A switch flips the
seats down and forward, al-
lowing easy entrance to the
rear. But legroom is skimpy
in the back, and if
you're six feet
tall, your head
will bump the
roof when the
Bug hits a pot-
hole. Even so, the
ride is much

THE NEW BUG \$16,500

Like its venerable
predecessor, this
Beetle is stronger
on style than
speed—but
it'll make
you smile

smoother than the old Bug's.
The hatchback trunk can ac-
commodate only a couple of
small suitcases, though the
rear seat handily folds down
for extra storage.

Air-conditioning, a six-
speaker stereo, front and side
air bags, and an antitheft sys-
tem are all standard. Options
include antilock brakes, pow-
er sunroof, leather seats, and
a four-speed automatic trans-
mission. The power-assisted
steering is light and respon-
sive, and the four-wheel disk
brakes grip well.

The Beetle's performance
is similar to that of the vw
Golf, on which it's based.
You'll initially have a choice
of two water-cooled engines,
located up front, instead of
the old Bug's air-cooled pow-
er plants in the back. The
base 2.0-liter unit puts out
115 horsepower but little low-
end power, so accelerating is
draggy. A 1.9-liter turbodiesel
is available as an option, but
performance-hungry buyers
may want to wait for a 1.8-
liter turbo due this fall—that
engine kicks out a far more
satisfying 150 horsepower.
The four-speed automatic
transmission (\$875 extra)

feels sluggish,
particularly accel-
erating uphill.
The five-speed
manual seems the
better choice. De-
spite all the glass
in the swooping
side windows,
wind noise is
pleasingly absent,
even at 80 mph.

In a market
flooded with ba-
nal designs and look-alike
models, the New Beetle
stands out from other sub-
\$20,000 autos. Spare me
the love beads and
peace signs, but the
car does hit an emo-
tional note. Driving it
isn't nearly as much
fun as, say, a Mazda
Miata. But if you
yearn for car that
makes you smile, there
is a lot to love in the
new Bug. *Bill Vlasic*

FUND WATCH

■ **SMALL STAR.** In Morn-
ingstar's 11th annual
selection of mutual-fund
managers of the year, the
well-known Mario Gabelli
won top honors. The big
surprise was
a runner-up:

John Bogle Jr.
and his N/I
Numeric
Investors
funds. Morn-
ingstar sin-
gled out the
obscure fund



family, with total assets
of just \$360 million,
because "when it comes
to commitment to share-
holders, few can match
Bogle," son of Vanguard
Group's senior chairman.

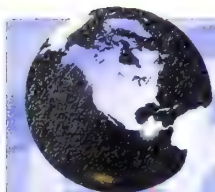
Morningstar was
impressed that N/I caps
expense ratios at 1% of
assets, below the average
1.4%. It also liked N/I's
conviction that small is
beautiful, demonstrated
last year when it closed
its Growth and Micro
Cap funds as assets
neared \$100 million.

"Fund companies are
effective when they're
small because they're
agile," says N/I founder
Langdon Wheeler.

Instead of doing the
usual company and indus-
try research, N/I (800
686-3742) uses computer
models to exploit stock-
price inefficiencies. From
their May, 1996, inception
to the end of 1997, N/I's
Growth fund returned an
annual average of 16.7%
and its Micro Cap fund,
30.8%. Two N/I funds
remain open: Growth &
Value and Larger Cap
Value. N/I's high-turnover
style may be best for
tax-deferred accounts
that can avoid short-
term capital gains
levies. *Robert Barker*

For an expanded version, go to
www.businessweek.com/today.htm or AOL, keyword: BW Daily.





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EDUCATION

Chief information officers of large corporations are overseeing the creation of a new world, online and within their companies. Corporate spending on information technology is rocketing to unheard of levels as every organization stakes its claim on a virtual storefront and rushes to turn powerful new processing technologies and software inventions into demonstrable competitive advantage. But how do you do that? One way to find direction is to talk with your peers. Now in its third year, *The Business Week Conference on THE DIGITAL ECONOMY* has become a prime meeting place for corporate technology leaders.

These pages offer an eye inside corporate computing's most exclusive gathering. You can put an ear into this tent too: visit <http://www.businessweek.com/execprog/digital> and listen in via RealAudio.

THE INTERNET: WHAT HAPPENS NEXT IS UP TO YOU

"Internet computing can change the way we work and live. But there is a risk that the Internet may make things worse instead of better. As business leaders, the decisions that we make during the next few years will dramatically affect the long term evolution of the Internet. We can use the Internet to increase communication, or increase censorship; to educate people, or to manipulate them; to broaden people's lives, or to narrow their points of view;

to unite people on a global scale, or to divide them. We are the generation whose decisions will set the direction of the emerging digital age. It is our responsibility to ensure that the Internet and the digital economy truly enhance and improve the way that we live and work. Or, to paraphrase John F. Kennedy, ask not what the digital economy can do for you. Ask what you can do for the digital economy."

Lewis E. Platt,
chairman, president,
and CEO,
Hewlett-Packard Company



**"Digital economy?
Digital marketplace?
The truth is, it's becom-
ing a digital habitat:
A full-fledged human
environment where
will all live and grow**

Lewis E. Platt,
chairman, president, and CEO,
Hewlett-Packard Company

CHEAP IN AMERICA, EXPENSIVE ELSEWHERE

"The real challenge in networks is the cost of the environment in North America and extending it to our operations in the rest of the world. We spend millions there for business only thousands here. So you end up with an organization that has information haves and have-nots."

John A. Roth, president and CEO,
Nortel (Northern Telecom)



by Scott Shuster, moderator of *The Business Week Conference on THE DIGITAL ECONOMY*

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EXECUTIVE PROGRAMS
second news intelligence

THE DIGITAL ECONOMY

PROCESSOR POWER
TO DOUBLE EVERY YEAR

"There are no technology limitations in the short term that will slow us down from delivering roughly twice as much processing power per year for the next 10 or 15 years. You can count on your fingertips what that will mean to you in terms of capability. I am a big fan of putting lots of processing power in the home. I think you'll see a lot of \$1,000 and \$1,500 PCs that are really very capable personal computers. By 1999, there will probably see more PCs than TVs being sold in the US. We have already reached that milestone here in the US."

R. Barrett, president and COO, Intel Corporation

SE, MAY I HELP
PLEASE?

"The Internet is driving a broadcast model where everything gets sent to everybody and the customer's equipment chooses the pieces important to them. This is happening because of the very high-speed circuits being put in place. More and more of the intelligence on the network will be pushed toward the edges, in some cases onto the premises of the business customers themselves. Traditional telephony finds it very difficult to deal with this. That is why a company like WorldCom believes they can be the Microsoft or the Intel of the communications business."

James T. O'Shea,
president, business
communications systems
and networking systems,
Technologies

TOWARD MORE
INTELLIGENT NETWORKS

"The Internet is driving a broadcast model where everything gets sent to everybody and the customer's equipment chooses the pieces important to them. This is happening because of the very high-speed circuits being put in place. More and more of the intelligence on the network will be pushed toward the edges, in some cases onto the premises of the business customers themselves. Traditional telephony finds it very difficult to deal with this. That is why a company like WorldCom believes they can be the Microsoft or the Intel of the communications business."

Bruce R. Bond,
president and CEO,
ANS Communications

AMAZON.COM:
HOW IT
ALL BEGAN

"In early '94 I came across this startling figure: 'Web usage growing 2300% per year.' I thought I would try to find a business plan that made sense in the context of that growth. I went through one process that led me to e-commerce and retailing. Then I asked the question, 'What is the first, best product to sell online?' Through a very deliberate forced ranking of about 20 different products, I finally picked books."

Jeff Bezos,
founder and CEO,
Amazon.com, Inc.



Dr. Eric Schmidt,
chairman and CEO, Novell, Inc.

THE SAME
RESULTS FOR
HALF THE MONEY?

"Ask a CIO if they feel they are getting value for their billions of dollars worth of IT spending, and most will probably answer no. If you ask most CEOs whether their investments are making their company strategy happen, making their company prosper, I think they'll say 'probably not.' There is clearly a set of applications that have impact. But one could ask whether we could get the same results spending half as much money. The answer is, we probably could."

Allan Z. Loren,
executive vice-president and CIO,
American Express Company

BUILT-IN INTELLIGENCE
COMES TO THE
UBIQUITOUS WEB

"Everywhere we look, networks matter. Customers around the world are deploying networks to transform every aspect of their business. We believe that the network is

quickly becoming the centerpiece of every computing endeavor. The challenge of the future will be to build increasingly intelligent, interconnected networks that enable enterprises to conduct completely new classes of activities and deploy entirely new kinds of applications."

THE DIGITAL ECONOMY

A TEN-FOLD INCREASE
IN SYSTEMS SPENDING

"When KPMG Peat Marwick combines with Ernst & Young, we will be 160,000 persons operating in our 150 countries, imparting and gaining knowledge from up to one third of the

world's leading businesses. But we are only as good as each individual. That is why it is essential that every individual share and gain knowledge from their peers across the whole organization. If we fail to achieve this we will be unable to aggregate our best practices. Over a three-year period, our costs for the technologies to accomplish this will exceed \$250 million. That is a ten-fold increase over three or four years ago, but it's worth it."

Roger S. Siboni, deputy chairman and COO, KPMG Peat Marwick LLP

THOSE CHAT
ROOMS WIELD
ENORMOUS POWER

"We used to have at least a chance to control the news about our companies, and how people perceived us. That's disappearing. Go on the web and look at the rumor chat rooms, the user group sessions about your products. Watch the minute-to-minute shift in people's opinions about your company. They have access to media stories, to SEC filings, to other customers. Today's spin control is like changing a tire while the car is moving. Of course, the leveling factor is that this also happens to your competition."

Carol Bartz, CEO and chairman, Autodesk, Inc.

CUSTOMERS ARE
CHOOSING NOT
TO SPEAK WITH A
HUMAN BEING

"At Cisco, the majority of our customers now prefer to contact us over the Internet, never speaking to a human being. For the first time the customer satisfaction level of talking to the system actually exceeded that of talking to a Cisco employee. We reached that milestone last month, after four years. Our average Internet application has resulted in over a 100% increase in productivity. That saves us about \$250 million a year on an expense base of \$2 billion."

John T. Chambers, president and CEO, Cisco Systems, Inc.

THE LOST GOLD MINES
OF INFORMATION

"Package applications like ours do a pretty good job receiving and holding data, but today that's not good enough. Sitting on your disk drives is an absolute gold mine of information that you have gathered, but not really used. That information can now be sliced and diced and made valuable to whole new classes of executives, including senior management. But the application vendors are behind the curve on this. If we are to be important strategic partners to our customers, we have to continue to provide the senior executive true information systems, not just transactional systems."

William Lawson, president, CEO, and founding partner, Lawson Software

HIGH TECHNOLOGY IS
NOT ENOUGH

"We are a technology company. That is our heritage. We used to measure how good we were by how many patents we had. Today, we have to be willing to open up and share those intellectual property rights, because in the digital economy the differentiation may no longer be whether my areal density is higher than the next disk's, but whether I have a complete solution to your specific problem. That will come not so much from the technological criteria of an individual component as from how we package it and put it together into the solution you need. That is where differentiation will be."

David E. Weiss, chairman, president, and CEO, StorageTek

ARE YOU APPLYING
MOORE'S LAW TO
YOUR BUSINESS
PROCESSES?

"We are now beginning to apply Moore's Law into the processes of organizations. You can expect your processes to be radically enabled every 18 months. The more we adapt our processes to the Moore's Law gains in processing power and the potential of the Internet, the more our business processes will speed up. But most corporations cannot even discuss this yet. It's not on their strategy table for conversation."

Richard Schroth, senior fellow, The Aresty Institute of Executive Education, The Wharton School



Smother Pavement for the Information Highway

"When you are trying to serve clients who need assistance from every part of your organization, then you have to connect with other parts of the world, standards become a huge preoccupation. It is very draining. It takes up a lot of psychological energy and it is a gigantic pain in the neck. This is why Microsoft is so powerful. We all try to go with a family or suite of things that supposed to work together."

Ed Marshall, managing director, technology, Bankers Trust Company

"The best thing for standards and for the future of interoperability is to have strong players like Microsoft. I know that's not a terribly popular thing to say, but honestly there are three standards in the world: Microsoft, Microsoft, and Microsoft. Look at the other efforts at standardization: They have been pathetic. But I can get everybody at my company working together if I use the de facto industry standard software."

Mac O'Reilly, vice-president, information systems, Wang Laboratories, Inc.

"Standards are one of those things that everybody wants but that everybody has to learn to live with or less without, realistically. There are a few cases where there is such enormous market dominance that there is a de facto standard. But then you get into business arrangements where you've got five other partners and they don't use the same thing, so you are always going to have to manage your way around the fact that standards just don't exist."

Ronald L. Paul, vice-president, technology and environmental affairs, Chevron Corporation

PETER DRUCKER: 'CFOs TO CONQUER CIOs'

"You call yourselves chief information officers, but you are not. You are chief data officers. If there is a chief information officer in your company, it is the chief accountant. I've been saying my friends in your business for years, you owe it to yourselves to pay attention to what is going on in accounting and to understand it. In 10 or 15 years from now our company will not have no information officers. There will be only one. The accounting people are ahead of you in understanding this."

Peter Drucker



SECRETS FROM THE LEADER OF ONE OF THE MOST VISITED SITES ON THE WEB*

"There are four components to building a successful Internet community.

The first is common interest.

That is what draws people together, whether at the personal or the commercial level. The second and most important component is the amalgam of contribution, effort, and participation. This is the litmus test of any community: The amount of work the members are willing to put into it. Third is feedback and interactivity. There has to be a way for members to know that through their effort they are indeed reaching others of similar interest. And fourth is a viable economic infrastructure, a complementary economic relationship among the members and the community organizer. One method we have used for this last piece is to figure out what people want for free, and then do more of that and charge."

*GeoCities.com is #7 after yahoo.com, ncscape.com, microsoft.com, excite.com, infoseek.com, and aol.com.

David Bohnett,
founder and CEO,
GeoCities

EXECUTIVE OPINION ON TECHNOLOGY MANAGEMENT ISSUES

Two hundred twenty-five senior technology executives at the *Business Week Conference on THE DIGITAL ECONOMY* offered their views on information technology management issues via a live polling system provided by Meridia Interactive. For more complete conference poll results, visit the *Business Week* website at www.businessweek.com/execprog/digital.

CIO POLL RESULTS

Our spending on information technology in 2000, as compared to 1997:

Triple or more:	10%
Double-to-triple:	21%
50%-100% increase:	24%
Less than 50% increase:	29%
Flat:	11%
Decline:	5%

I am planning my company's information systems spending:

Three years out:	21%
Two years out:	32%
One year out:	34%
Six months out:	6%
Just doing it:	7%

My CEO enthusiastically pursues new opportunities made possible by advances in information technology.

Yes, enthusiastically:	55%
Pursuing, not enthusiastically:	20%
Little progress, lip service, no real budget:	20%
No movement at all:	5%

As CIO, I am part of my CEO's top level strategy-setting team.

Yes:	51%
Consulted, but no 'seat-at-the-table':	29%
No:	20%

We have a clearly delineated Internet strategy.

Yes:	39%
No:	61%

In hall polling provided by Meridia Interactive, (610) 260-6800

INTERNET

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can reach people who
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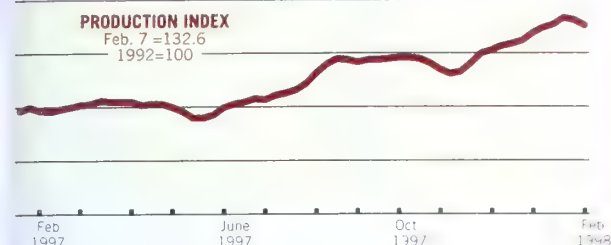
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Business Week Index

PRODUCTION INDEX

Change from last week: -0.4%
Change from last year: 6.4%



The production index continued its slide, as did the unaveraged index which fell 0.4%, from 133.1 to 132.6 in the week ended Feb. 7. After seasonal adjustment, auto production was down 11.3% and trucks 4.3%. Output was down at all three big auto makers—Ford posted a 2.3% decline, GM was down 1%, and Chrysler fell 8.2%. Steel, lumber, and rail freight were also down. Reasons were posted for the production of coal, oil, and electric power.

Production index copyright 1998 by The McGraw-Hill Companies.

LEADING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STOCK PRICES (2/13) S&P 500	1020.90	1012.46	26.3
CORPORATE BOND YIELD, Aaa (2/13)	6.69%	6.69%	-7.9
INDUSTRIAL MATERIALS PRICES (2/13)	95.7	96.0	-11.4
MONEY SUPPLY, M2 (2/2) billions	\$4,080.5	\$4,070.6r	6.0
INITIAL CLAIMS, UNEMPLOYMENT (2/7) thous.	303	305r	-1.6
MORTGAGE APPLICATIONS, PURCHASE (2/13)	222.5	249.4	33.0
MORTGAGE APPLICATIONS, REFINANCE (2/13)	1,685.7	2,028.7	319.9

Sources: Standard & Poor's, Moody's, Journal of Commerce (Index: 1990=100), Federal Reserve, Labor Dept., Mortgage Bankers Assn. (Index: March 16, 1990=100)

INTEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
FEDERAL FUNDS (2/17)	6.00%	5.44%	5.55%
COMMERCIAL PAPER (2/17) 3-month	5.45	5.42	5.38
CERTIFICATES OF DEPOSIT (2/18) 3-month	5.53	5.55	5.34
FIXED MORTGAGE (2/13) 30-year	7.20	7.16	7.85
ADJUSTABLE MORTGAGE (2/13) one-year	5.76	5.70	5.81
TIME (2/13)	8.50	8.50	8.25

Sources: Federal Reserve, HSH Associates, Bloomberg Financial Markets

Raw data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (2/14) thous. of net tons	2,232	2,167#	7.8
AUTOS (2/14) units	115,570	112,288r#	-7.9
TRUCKS (2/14) units	142,352	135,236r#	12.5
ELECTRIC POWER (2/14) millions of kilowatt-hrs.	NA	64,943#	NA
CRUDE-OIL REFINING (2/14) thous. of bbl./day	NA	14,154#	NA
COAL (2/7) thous. of net tons	21,027#	20,564	-5.4
LUMBER (2/7) millions of ft.	471.1#	477.8	-5.2
RAIL FREIGHT (2/7) billions of ton-miles	26.5#	26.8	-1.5

Sources: American Iron & Steel Institute, Ward's Automotive Reports, Edison Electric Institute, American Petroleum Institute, Energy Dept., WWP1, SFP2, Association of American Railroads

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (2/18) \$/troy oz.	298.150	298.450	-13.9
STEEL SCRAP (2/10) #1 heavy, \$/ton	140.50	140.50	-4.1
COPPER (2/13) ¢/lb.	79.4	80.2	-28.8
ALUMINUM (2/13) ¢/lb	72.0	72.8	-3.7
COTTON (2/13) strict low middling 1-1/16 in., ¢/lb.	64.41	63.65	-8.0
OIL (2/17) \$/bbl.	15.41	16.18	-30.4
CRB FOODSTUFFS (2/17) 1967=100	224.01	225.34	-6.0
CRB RAW INDUSTRIALS (2/17) 1967=100	299.21	295.52	-13.3

Sources: London Wednesday final setting, Chicago market, Metals Week, Memphis market, NYMEX, Commodity Research Bureau

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (2/18)	126.29	123.67	124.39
GERMAN MARK (2/18)	1.82	1.82	1.70
BRITISH POUND (2/18)	1.64	1.63	1.61
FRENCH FRANC (2/18)	6.10	6.10	5.74
ITALIAN LIRA (2/18)	1796.0	1795.5	1690.4
CANADIAN DOLLAR (2/18)	1.43	1.44	1.36
MEXICAN PESO (2/18)	8.531	8.435	7.777
TRADE-WEIGHTED DOLLAR INDEX (2/18)	109.6	108.9	105.0

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars. Trade-weighted dollar via J.P. Morgan

THE WEEK AHEAD

FEDERAL BUDGET

Monday, Feb. 23, 2 p.m. EST ▶ The Treasury Dept. will probably announce a surplus of \$2 billion in January, says the median forecast of economists surveyed by Standard & Poor's MMS, a unit of The McGraw-Hill Companies. That's bigger than the \$13.4 billion deficit of January, 1997. The Clinton administration has predicted a \$10 billion plus for fiscal 1998.

EMPHREY-HAWKINS TESTIMONY

Tuesday, Feb. 24 ▶ Federal Reserve Chairman Alan Greenspan will give his semiannual testimony on monetary policy and the economic outlook before the House of Representatives. He is scheduled to repeat

his testimony before the Senate on Feb. 25.

CONSUMER PRICE INDEX

Tuesday, Feb. 24, 8:30 a.m. EST ▶ Consumer prices of all goods and services probably increased by just 0.1% in January, says the MMS forecast, the same as in December. Excluding food and energy, core prices likely rose 0.2%, also as in December. Beginning with this report, the Labor Dept. will introduce a new geographic-area sample, revised categories, and updated expenditure weights.

CONSUMER CONFIDENCE

Tuesday, Feb. 24, 10 a.m. EST ▶ The Conference Board's index of consumer confidence

likely rebounded to 129.5 in February, after falling nine points in January, to 127.3.

DURABLE GOODS ORDERS

Thursday, Feb. 26, 8:30 a.m. EST ▶ New orders for durable goods probably increased 1% in January, after a drop in transportation equipment bookings led a 6.1% plunge in December orders.

GROSS DOMESTIC PRODUCT

Friday, Feb. 27, 8:30 a.m. EST ▶ The MMS median forecast expects only a small revision in economic growth in the fourth quarter. Real GDP likely grew at a 4.1% annual rate, instead of the 4.3% pace reported by the Commerce Dept. a month ago.

This Week, Online

Business Week presents frequent live conferences and chats on America Online—your opportunity to ask questions about features from the magazine.

ONLINE
BusinessWeek

Monday

Is your company in need of a fix? Call in Renee Fellman, a turnaround expert who has helped many small and midsize companies snap back. She'll be online to help with your problems. **Feb. 23**
8 p.m. ET in the BW Enterprise Chat Room

Thursday

The Year 2000 problem will cost you—and the U.S. economy—a lot more than you may think. BW Economics Editor Michael J. Mandel leads a discussion of this disturbing Cover Story. **Feb. 26**

9 p.m. ET in BW Online's Conference Room

AOL keyword: BW Talk

Transcripts of all conferences are available for downloading from the BW Online area on AOL soon after each event.

Index to Companies

This index gives the starting page for a story or feature with a significant reference to a company. Most subsidiaries are indexed under their own names. Companies listed only in tables are not included.

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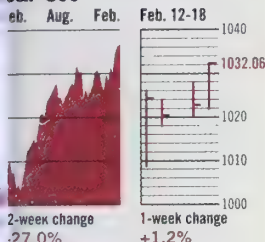


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Investment Figures of the Week

STOCKS

S&P 500



IMMUNITARY

bulous February: U.S. stocks e on one heck of a winning eak. On Feb. 18, the Dow sed at 8451.1, the sixth new gh in a row. The S&P 500 ck index looked equally art, at 1032.1, also its sixth w high in as many days. all- and mid-cap stocks are mbing as well, but they can't ep up with the blue chips. pling stocks were economic dicators that depict a slowing onomy and lower interest tes. Looking abroad, Euro-an stocks rallied along with e U.S., while Asian and Latin erican markets stumbled.

U.S. MARKETS

	Latest	% change Week	Year
Dow Jones Industrials	8451.1	1.6	20.4
NASDAQ Combined Composite	1715.7	0.4	25.6
S&P MidCap 400	346.6	1.1	28.8
S&P SmallCap 600	190.0	0.9	27.8
S&P SuperComposite 1500	221.4	1.2	27.2

SECTORS

	Latest	% change Week	Year
Bloomberg Information Age	322.8	0.4	29.3
S&P Financials	124.1	1.8	29.5
S&P Utilities	231.8	1.2	16.3
PSE Technology	329.4	1.1	22.4

FOREIGN MARKETS

	Latest	% change Week	Year
London (FT-SE 100)	5723.4	2.1	31.3
Frankfurt (DAX)	4628.8	0.9	43.1
Tokyo (NIKKEI 225)	16,613.9	-3.4	-10.7
Hong Kong (Hang Seng)	10,671.0	-1.1	-18.6
Toronto (TSE 300)	6944.2	0.0	11.1
Mexico City (IPC)	4550.2	-3.8	17.4

FUNDAMENTALS

	Latest	Week ago	Year ago
S&P 500 Dividend Yield	1.51%	1.49%	1.78%
S&P 500 P/E Ratio (Last 12 mos.)	26.1	25.8	21.4
S&P 500 P/E Ratio (Next 12 mos.)*	20.1	20.0	17.2
First Call Earnings Revision*	-3.43%	-4.18%	-0.34%

TECHNICAL INDICATORS

	Latest	Week ago	Reading
S&P 500 200-day average	929.6	925.0	Positive
Stocks above 200-day average	66.0%	67.0%	Neutral
Options: Put/call ratio	0.55	0.51	Negative
Insiders: Vickers Sell/buy ratio	1.58	1.59	Positive

Data: Bloomberg Financial Markets; *First Call Corp.

BEST-PERFORMING GROUPS

	Last month%	Last 12 months%
Defense Electronics	23.6	Specialty Appr. Retailers 81.0
Manufactured Housing	21.7	Manufactured Housing 77.6
HMOs	21.4	Airlines 74.1
Machine Tools	20.1	Specialty Retailers 62.4
Medical Prods. & Supps.	16.7	Genl. Merchandise Chains 61.7

WORST-PERFORMING GROUPS

	Last month%	Last 12 months%
Tobacco	-6.3	Engineering & Constr. -40.4
Hospital Management	-2.2	Shoes -40.3
Pollution Control	-1.8	Metals -40.1
Oil-Well Equip. & Svcs.	-1.0	Gold Mining -35.2
Domestic Oil	-0.5	Photography/Imaging -27.7

BLOOMBERG MONEY FLOW ANALYSIS

Rebound ahead? Stocks with most significant buying on price weakness

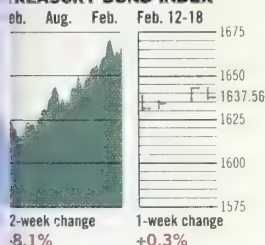
	Price	1-month change
AT&T	63 7/8	-1 1/16
IBM	102	-6 3/8
Wells Fargo	324 1/2	-5 1/4
Sun Microsystems	44 7/8	-2 9/16
American Home Products	89	-5 1/4
Gillette	102 1/16	-1 1/16

Decline ahead? Stocks with most significant selling on price strength

	Price	1-month change
Microsoft	154 7/8	16 9/16
Cisco Systems	64 15/16	5 7/16
Intel	84 5/8	8 3/8
Oracle	25 5/8	5 3/8
WorldCom	38	6 1/2
Applied Materials	36 3/8	5 5/8

INTEREST RATES

TREASURY BOND INDEX



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KEY RATES

	Latest week%	Week ago%	Year ago%
MONEY MARKET FUNDS	5.16	5.16	4.96
90-DAY TREASURY BILLS	5.18	5.20	5.11
6-MONTH BANK CDS	5.09	5.08	5.01
1-YEAR TREASURY BILLS	5.26	5.27	5.46
10-YEAR TREASURY NOTES	5.48	5.56	6.30
30-YEAR TREASURY BONDS	5.83	5.84	6.57
LONG-TERM AA INDUSTRIALS	6.46	6.50	6.99
LONG-TERM BBB INDUSTRIALS	6.91	6.96	7.39
LONG-TERM AA TELEPHONES	6.74	6.76	7.27

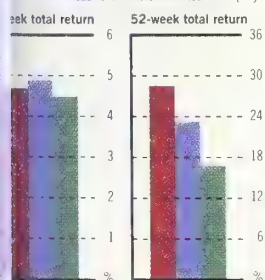
BLOOMBERG MUNI YIELD EQUIVALENTS

Taxable equivalent yields on AAA-rated, tax-exempt municipal bonds, assuming a 31% federal tax rate.

	10-yr. bond Latest week	Last week	30-yr. bond Latest week	Last week
GENERAL OBLIGATIONS	4.28%	4.33%	4.86%	4.91%
PERCENT OF TREASURIES	78.11	77.75	83.34	84.01
TAXABLE EQUIVALENT	6.20	6.28	7.04	7.12
INSURED REVENUE BONDS	4.41	4.44	5.08	5.11
PERCENT OF TREASURIES	80.48	79.73	87.11	87.43
TAXABLE EQUIVALENT	6.39	6.43	7.36	7.41

MUTUAL FUNDS

S&P 500** U.S. Diversified All Equity



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EQUITY FUNDS

Leaders

Four-week total return	%	Laggards	%
DFA Japanese Small Co.	22.9	Matthews Korea I	-13.6
DFA Pacific Rim Small Co.	18.2	American Heritage	-12.0
Montgomery Gl. Commun. R	16.6	Prudent Bear	-11.3
U.S. Global Inv. China Reg.	15.6	Wright EquiFd.-Mexico	-6.2
Cockville Intl. Value	14.7	Lexington Troika Russia	-5.5

Laggards

52-week total return	%	Laggards	%
Munder Micro-Cap Eqty. Y	59.4	Matthews Korea I	-59.7
Fidelity Sel. Air Trans	54.2	U.S. Global Investors Gold	-58.6
Delaware Aggressive Gr. A	51.8	Midas	-58.5
Fidelity Select Retailing	50.8	Bull & Bear Gold Investors	-56.6
Janus Special Situations	49.5	Invesco Strategic Gold	-56.2

EQUITY FUND CATEGORIES

Leaders

Four-week total return	%	Laggards	%
Technology	8.4	Real Estate	-1.1
Pacific/Asia ex-Japan	6.4	Natural Resources	1.5
Europe	6.3	Utilities	1.7
Precious Metals	6.1	Latin America	2.1
Unaligned	5.6	International Hybrid	2.2

Laggards

52-week total return	%	Laggards	%
Financial	34.5	Precious Metals	-40.7
Communications	30.8	Pacific/Asia ex-Japan	-38.3
Unaligned	28.8	Diversified Pacific/Asia	-26.5
Small-cap Value	27.4	Diversified Emerging Mkts.	-16.3
Mid-cap Value	25.5	Japan	-7.7

Data are as of market close Wednesday, Feb. 18, 1998, unless otherwise indicated. Industry data include S&P 500 companies only. Fundamentals, technical indicators, Bloomberg mon-

itor flow analysis, and mutual fund returns are as of Feb. 17. For a more detailed explanation, write to us or E-mail figures@businessweek.com. r=revised **Vanguard Index 500 Fund

PANIC IN THE YEAR 2000

For the economy, the Year 2000 software problem has already arrived. The good news is that the pell-mell race to fix the Y2K bug is pumping up capital spending and tightening the job market for any college kid who can write code. The bad news is that fixing the first-ever global glitch in information technology will take half a percentage point off gross domestic product growth in 2000, reduce productivity growth, and raise inflation (page 92). But that's under a best-case scenario. Odds are, given the enormous complexity of the problem, the economic impact will be worse. For individual companies and government agencies, such as the Internal Revenue Service, the situation could be a disaster.

Corporate America has no excuse for taking so long to face Y2K. The enormity of the problem has been known for years. There are 40 years of software "out there," made up of billions of lines of code spread over different programming languages, operating systems, databases, and hardware platforms. It isn't enough for a corporation to debug its own software. It must synchronize with all its vendors, suppliers, and customers in every town and village in every country around the world. Not only must the changes be made, they must be made in exactly the same way. Or computers will crash. If a small regional German *landesbank*, for example, chooses a different method to solve its Y2K problem than, say, Citibank, their computer systems could corrupt each other as the banks trade currencies. Ditto for a Taiwanese motherboard manufacturer that supplies Dell Computer or Compaq Computer.

The complexity of the Y2K problem boggles the mind, which is perhaps why Washington has been so slow to deal with it. The General Accounting Office reports that 16 of 27

major government agencies are planning to complete the debugging of critical software by November or December, 1999. That leaves only weeks for crucial testing of extremely complex computer systems and almost guarantees breakdown. Some 60 senior corporate executives—from companies including Texas Instruments, Unilever, Ford, Bombardier, and Lloyds TSB Banking—recently warned President Clinton and the Prime Ministers of Britain and Canada that government failure to solve Year 2000 problems could produce "delays in welfare payments, the triggering of financial chaos by breakdown in revenue collection and debt management, and malfunctions in the air traffic control and defense systems."

Dealing with the Y2K bug is already bending the U.S. economy out of shape. An army of software writers is busy fixing old programs instead of developing new ones, hurting productivity. An army of attorneys is getting ready to step to cash in on Year 2000 liability when computers start crashing. Real wages in the management consulting and accounting businesses are rising at a fast clip, pulling up the national average. But if the Federal Reserve tightens monetary policy in 1998 or 1999 to battle wage inflation, it risks tipping the economy into recession later, at its most Y2K vulnerable.

The Y2K shock is probably the first of many new and unexpected high-tech jolts that will hit the economy in the decades ahead. This one is entirely predictable and should have been totally manageable. Yet it was not. That should be a warning: As the U.S. shifts from an industrial to an information-based economy, technology is likely to affect growth and the business cycle as much, if not more, than more familiar variables. In the New Economy, the business cycle is the child of innovation and product development.

WE DON'T NEED CONTROLS ON GLOBAL CAPITAL

Is the Asian financial crisis actually a crisis of global capitalism? To a growing chorus, including Japan's Vice-Minister of Finance Eisuke Sakakibara, hedge fund manager George Soros, and Malaysia's Prime Minister Mahatir, the answer is "yes." They believe there is a need for a new "architecture" of global financial institutions to govern capitalism today. They argue that globalization has unleashed uncontrollable amounts of capital that swamp national economies, destroying growth and jobs in their wake. Bolstering the International Monetary Fund is necessary but not sufficient. New institutions, laws, and taxes must be created to tame global capital.

We don't think so. The truth is that Asia's command-and-control economic systems were able to harness double-digit savings rates to generate high growth rates for nearly three decades. Poverty was cut dramatically. It came to a halt in Asia because the corrupt, hierarchical economies could no

longer efficiently allocate capital, whether internally generated or from overseas. The Korean *chaebol* or the Southeast Asian family conglomerates overborrowed to build overcapacity because they received cheap financing from politicians or relatives. Even now, the *chaebol* are getting subsidized loans from friendly Korean banks to hang on to uncompetitive operations (page 54).

A new global financial architecture will not solve these problems. Global capital should be free to move but must be made to pay for its mistakes. One lesson the Asian crisis teaches is that capital flowed to Indonesia, Thailand, and Korea regardless of obvious risk.

Painful as it is, the Asian crisis is acting as a solvent breaking down authoritarianism in one country after another. In making markets more flexible and robust, societies more democratic. Global capitalism is doing what it has done for centuries—destroying the old, creating the new. It is not in crisis.

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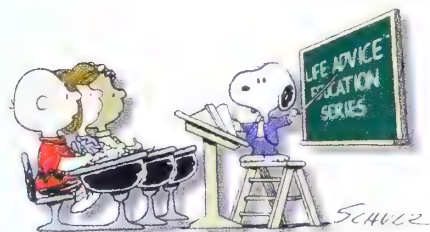


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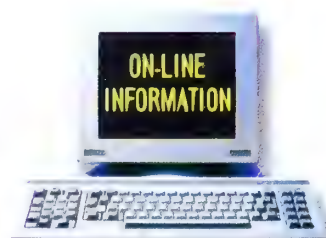
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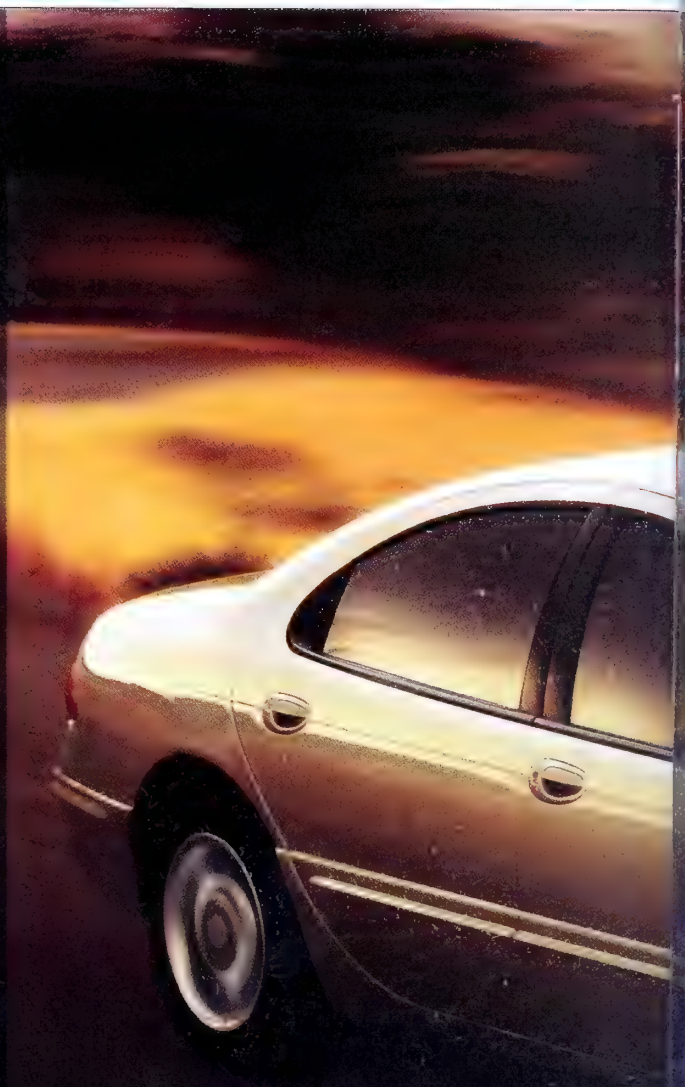
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Cover Story

70 McDONALD'S TARNISHED ARCHES

The fast-food legend, a pacesetter in American taste for decades, is losing its dominance. Customers complain about the food. New products flop. Franchisees are angry. Management and the board are entrenched. And results are poor: McDonald's share in fast-food sales is slipping, its stock is stagnant, and operating profits lag inflation. Can it get back on course and regain its edge?

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TO THE RESCUE

Richard Scrushy
hopes to revive
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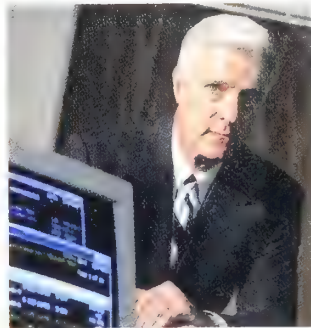
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Up Front

EDITED BY ROBERT McNATT & LARRY LIGHT

ASIAN FLU

A PROTECTIONIST CHANGES HIS STRIPES

HERE'S A CONCEPT FOR you: Dick Gephardt as poster boy for IMF bailouts. Although he's considered the most prominent protectionist in the House, Minority Leader Gephardt now backs passage of the \$18 billion aid package for the International Monetary Fund.

He is working closely with Treasury Secretary Robert Rubin to pass the bill, which is designed to help the IMF prevent an Asian financial meltdown. In the past, Rubin and Gephardt have clashed over trade issues such as the NAFTA deal.



PRO-IMF: Gephardt

But those differences have been pushed aside. Rubin now calls Gephardt "a key leader in helping to forge a bipartisan consensus on this important issue."

Why the change of heart? Gephardt believes an Asian collapse will hurt U.S. job growth. He also wants to shed his protectionist label and broaden his base for a possible Presidential race. So he will talk about the issue on Mar. 3 to the

Council on Foreign Relations. Then he'll head to Wall Street and urge business leaders to lobby on the IMF's behalf. *Richard S. Dunham*

VOX POPULI

A NATION OF HAPPY FACES

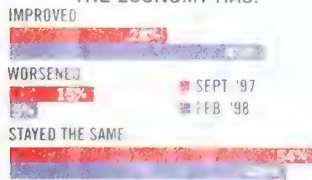
WHO'S WRINGING THEIR hands over the fallout from Asia and other potential economic problems? Not the average American. Increasingly, folks say they're pleased with the economy's recent performance and are optimistic about the future,

past 12 months. When people were asked the same question back in September, only 28% of them said that it had improved.

While many economists predict a slowdown later in 1998, Americans feel things will continue to go swimmingly. Peering ahead, 30% in the February survey thought the economy will improve and 53% said it would stay the same, which is to say pretty good. Those sanguine numbers are similar to the way folks saw the future five months ago.

Personally, Americans believe that they are doing very well. An impressive 51% of those surveyed expect that their families to be better off financially in the next 12 months. Only 7% predicted that their families would be worse off, with the rest saying their fortunes would remain the same. □

PERCENT OF PEOPLE SAYING THE ECONOMY HAS:



according to a survey of 999 adults by Louis Harris & Associates for BUSINESS WEEK.

The poll, taken Feb. 18-23, found that 45% felt the economy had improved during the

TALK SHOW "I think I can do business with him. And I think he was serious."

—U.N. Secretary General Kofi Annan, on his agreement with Saddam Hussein.



BITTER PILL: Fees unrealized

Britain's *Acquisitions Monthly*. But the biggest losers are the investment bank that worked on

THE DEAL MILL

SMITHKLINE: OLDER, WISER—AND POORER

WHEN CORPORATIONS DON'T get hitched, it can cost a bundle. Twice, within less than a month, SmithKline Beecham has had second thoughts at the altar, as merger proposals with American Home Products and then Glaxo Wellcome fell through. The failed courtships will cost the company, and its investment bankers, millions.

In the latest breakup, SmithKline and Glaxo may have rung up as much as \$32 million in banking, legal, and public-relations fees, estimates

the deal. Morgan Stanley Dean Witter, Discover represented SmithKline Beecham while Lazard Frères advised Glaxo. By some industry estimates, those two firms might have earned \$160 million in fees had the merger gone down.

The bankers involved won't comment on the record, but one close to the talk says: "Some advisers are desperate to do deals, but those who try to retain a measure of objectivity try not to force people to do deals against their wishes." Translation: It's more important to retain the confidence of a lucrative client than to consummate a deal. And \$32 million ain't chump change. *Stanley Rees*

SOFTWARE HARDBALL

NOT YET CLEARED FOR TAKEOVER

WILL NATIONAL SECURITY concerns doom Computer Associates International's \$9 billion hostile bid for Computer Sciences Corp.? CSC consults for the Pentagon, CIA, and National Security Agency. A healthy chunk of its \$1.1 billion in defense work is classified.

But a foreign national, Walter Haefner of Zurich-based Cereol Holding, holds a 23% stake in CA, acknowledges the company. CSC lawyers are studying whether his ownership might endanger some of its eyes-only business under Pentagon rules that restrict security clearances for foreign-owned

firms. "Foreign ownership will clearly trigger national security reviews," says James McAleese, a defense industry lawyer.



MIFFED: CA's Wang

Haefner's stake may not bar the deal, though. Computer Associates says that he is only a passive investor. And Charles Wang, chairman and CEO of CA, notes that it is already cleared for some classified business anyway. CSC has hauled its foe into court to stop the merger. Now, any further national security review could cause further delay. As for Wang, he says the security issue "is just a smokescreen." *Stan Crook*

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Up Front

SLUGFESTS

THIS TIME, THE EMPIRE MAY STRIKE OUT

IN THE CORPORATE WORLD, George Lucas is something of a Darth Vader. No one drives a harder deal for rights to the characters he creates. But after strong-arming toymakers into a pair of record-breaking deals, Lucas is feeling the dark side of the Force.

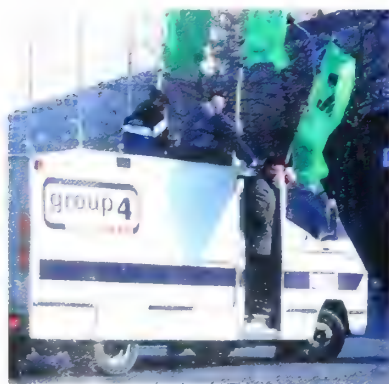
Last year, he sought bids for rights to market toys based on his next three *Star Wars* films. By offering Lucas equity on top of royalty payments, Hasbro and Galoob Toys, the current licensees, won. But along the way, Galoob neglected its other big licenses, including *Men in Black* and National Football League figures. All flopped, says Gary Jacobson, an analyst at Jeffries & Co.



As a result, Galoob's stock fell to about \$8.30 a share from \$24, making Lucas' warrants to buy 20% of the company at \$15 a share worthless.

And Galoob, now in the red, has run through most of its cash. So it most likely will borrow \$40 million for the first installment of a \$140 million royalty fee. The question is whether it can secure a loan by Memorial Day, 1999, when the first of the new *Star Wars* movies opens. Its lender, Bankers Trust, has already walked away.

So for of all his tough bargaining, in the end, Lucas may wind up with little to collect from Galoob. Neither he nor Galoob would comment. *Kathleen Morris*



OVER THERE

I HOPE THE PARKING METERS TAKE VISA

IF YOU WANT TO SEE A cashless society, go to Belgium. Thanks to a strike by armored-car guards—just ending after six weeks—hard currency has been in short supply. ATMs sported "Out of Money" signs, and cabbies and restaurant owners com-

CASH CRISIS: Armored-car guards on strike

plained about too many charge cards. "Vacationers couldn't get cash, either," says Viviane Huybrecht of Kredietbank.

The unhappiest Belgians were those in the underground economy. With the country's high tax rates, a lot of business, such as construction work, is handled on a cash basis to avoid tax collectors. A Kredietbank customer, says Huybrecht, became furious when he couldn't cash a \$15,000 money order. "He later admitted the money came from black-market work," she says. If the man deposited the funds, he risked paying taxes on them. Too bad the strike is ending. The government might have finally found a way to make its citizens honest. *William Echikson*

DRAWN & QUARTERED



PRODUCT PEEK

PACKING HEAT—AND A BIG WHEEL, TOO

CAN SMITH & WESSON MAKE A high-caliber bike? The pistol maker is gunning to be a big wheel by introducing its own police bicycle. But the response from cycle cops has been less than arresting.

"My initial reaction was, 'What does Smith & Wesson know about bikes?'" says Sergeant Tom Northfell of Chicago's 21-officer Police Bicycle Patrol Unit, which uses rival Trek. S&W, for instance, first used cheaper parts, but found they wouldn't hold up and has since upgraded them.

S&W has sold about 300 cop bikes since January—but with only passing help from bike maker Murray Ohio Manufacturing, also owned by British



S&W: Now into bikes

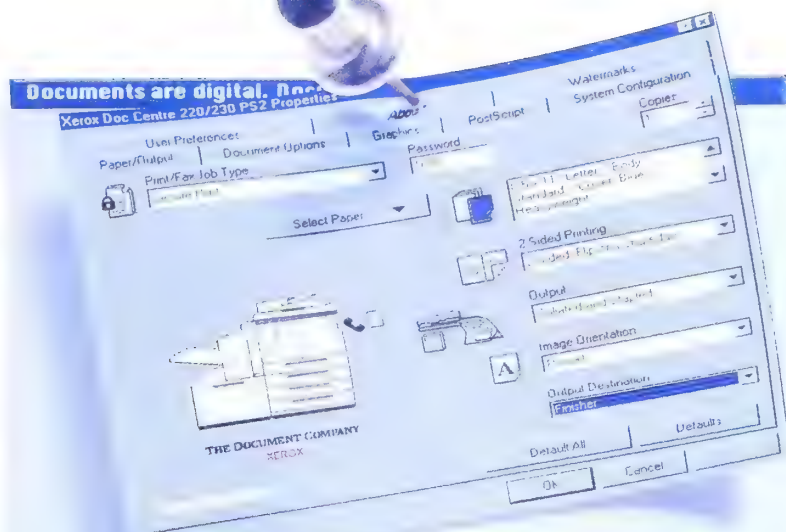
concern Tomkin PLC. Aside from providing entrée to parts makers "They've done nothing for me of the bicycle line," says S&W executive David Sargeant. But, he adds, S&W didn't mind to much: Murray makes lots of kids' bikes—evoking images of pin frames and flowered baskets. And that, notes Sargeant, is just not how cops see themselves. *Roy Furchgo*

THE BIG PICTURE

SEED MONEY IS SPROUTING Venture capital investing, a wasteland in the early 1990s, is blooming anew. VC funds, which invest in fledgling businesses in return for an equity stake, have become so popular that the average fund grew to \$89 million last year, from \$12 million just one year earlier.



FOOTNOTES Employees who leave their jobs because they don't like the company: 20%; those who leave for more money: 63%



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ONE AMWAY DOUBTER —AND ONE TRUE BELIEVER

So much for minimizing advertising and eliminating the middleman. Direct-to-consumer, multilevel marketers such as Amway Corp. don't seem to pass the savings on to their agents or distributors, who are the prime consumers of their products ("Amway II: The kids take over," People, Feb. 16).

In addition, Amway prices are often much higher than those of similar products in the conventional retail marketplace. Such marketers try to package their goods in a way that makes them seem unattainable elsewhere. They say the products are concentrated—so that less is needed. Sometimes, they claim they contain rare ingredients. They advise customers to minimize their use of the products—but seem to rely on use being hard to reduce.

P.T. Barnum said: "There is a sucker born every minute," and that's more than enough, it seems, to keep the pipeline of new recruits full for multilevel marketing of every possible stripe.

Thomas D. East
 Bryn Mawr, Pa.

Some facts you overlooked: You didn't mention that Amway had created more millionaires and financially independent people than any other company in the U.S. Yes, you are going to have some people who don't succeed, but that's true with any business.

Then you mentioned motivation. Most Americans don't know what it is like to have something positive in their lives. It's nice to be around winners who encourage you and work with you so you can have an opportunity to take care of your family.

Amway is not for everyone, because it requires change. But for those who want something better for themselves and their families, you will not find another business opportunity that not only helps you grow financially but also in all other aspects in your life.

Robert Strong III
 Bothell, Wash.

CORRECTIONS & CLARIFICATIONS

In "Mr. House finds his fixer-upper" (People, Feb. 2), we misnamed Petrus Williams, networking director at DreamWorks SKG.

"Warp speed ahead" (Information Technology, Feb. 16) should have stated that most cable-modem users can send data back to the Internet over cable systems. Also, cable data services, such as @Home Corp., offer PC users transmission speeds of up to 384 kilobits per second from their PCs to the Internet.

PRaise for THE DOW JONES/NBC DEAL

Your article on Dow Jones & Co. new global business television alliance with NBC characterized the deal as "little examined" ("Dow Jones: Bright lights, big mistake," News: Analysis & Commentary, Feb. 23). In fact, had you checked, you would have found recent discussions of the alliance in reports by three of the analysts who cover Dow Jones.

Here is what the analysts have said: Steven N. Barlow of CS First Boston wrote: "We applaud the joint-venture arrangement." In addition, Lauren Ric Fine of Merrill Lynch & Co. called it a "logical step" and said that the deal "makes enormous sense. Value being surfaced." Susan L. Decker of Donaldson, Lufkin & Jenrette Inc. termed the deal "value-enhancing" for Dow Jones. "The alliance is structured as a 50-50 joint venture," she noted, "with Dow Jones receiving fully half of the economic benefits (despite less than 100% ownership of ABN and EBN). The alliance should substantially improve distribution and promotion capabilities."

A postscript: Your story raised the question of, but didn't address, Dow Jones's growth strategy. You were told but didn't tell readers, that a key component of that strategy is Dow Jones Indexes—the direct competitor of a up

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L'S BUSY SCHEDULE NIKE'S DOING

é vs. Nike: Guess who won't
(Sports Business, Feb. 16) does
curately represent Nike Inc.'s re-
ship with the Confederation of
an Football (CBF) and our role in
an football. It does, however, point
elé's ongoing role as a global
man for a competing brand.

ttle over a year ago, Nike became
nsor of the CBF. Since then, we
been accused of adding unneces-
xhibition matches to Brazil's pre-
Cup '98 schedule. Nothing could be
r from the truth. As defending
hampion, Brazil received an auto-
invitation to World Cup '98 and
t involved in the qualifying process
s event. So an ambitious schedule
endlies" was developed by the CBF
hampion would be prepared to
its title. None of the matches
unnecessary additions: The team
have played someone, somewhere,
f Nike were not a team sponsor.

Keith G. Peters
Communications Director
Nike Europe
Hilversum, Netherlands

T: ONE ANALYST DOESN'T A GOOD YEAR

ironic. We're leading the telecom-
ations revolution and pioneering
ure of how voice, data, and multi-
will be delivered. Yet there's one
we can't change: We can't make
ers get their facts straight.

'Pick up this call. Hang up that
Inside Wall Street, Feb. 23), Gene
rcial quotes investment manager
Lappin on Qwest Communications
national stock. Marcial relies on
n as the sole basis of his story,
Lappin is uninformed about Qwest's
gy. Our advanced multimedia fiber-
network, enabling the introduction
v services, has been lauded by fi-
analysts and has proved effective
customers. In addition, Marcial's
suggests that revenues and earn-
om our construction-services com-
are not meaningful despite the
hat we have been applauded for
erving shareholder capital.

set the record straight, Qwest re-

ported a very strong yearend. We re-
ported a fourth-quarter revenue increase
of 104% from the same period in 1996
and a full-year revenue increase of
202%. Communications-services revenue
increased 80% from the fourth quarter
in 1996 and 58% for the full year. We're
well on the way to making the trans-
mission of multimedia data and video
as easy as voice. We only wish Marcial

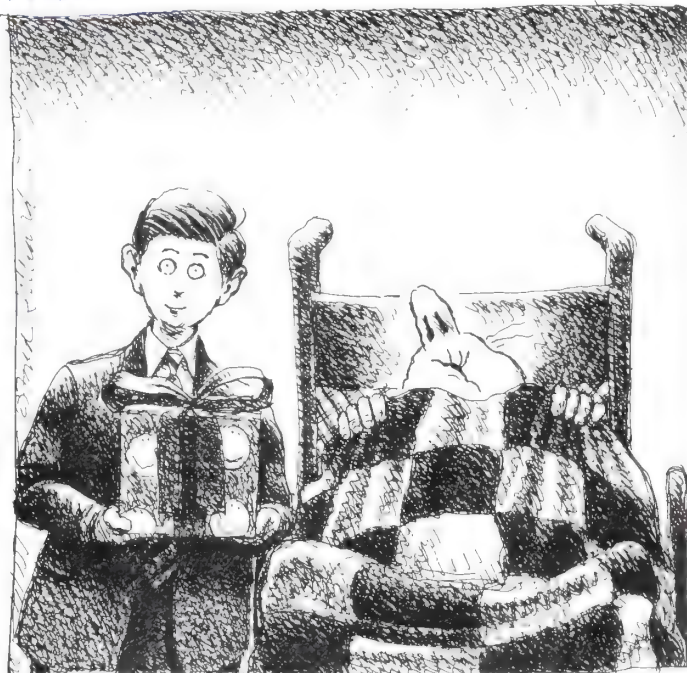
or Ms. Lappin had picked up the phone.

Joseph P. Nacchio, CEO
Qwest Communications International
Denver

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tions in defense of 50 million consumers.

If Steven V. Brull ("Smoke-filled lobbyists were here," News: Analysis & Commentary, Feb. 16) had looked, he would have discovered a citizens' rebellion against the California smoking ban that would be impossible to dismiss as some kind of political manipulation.

Jeanie R. Austin

David M. Nummy

Charles W. Sydnor Jr.

National Smokers Alliance

Alexandria, Va.

WHY GOVERNMENT GRIDLOCK IS A GOOD THING

Howard Gleckman provides insight into how far tax breaks and entitlement programs have come in the past 30 years ("Break the tax-break habit," News: Analysis & Commentary, Feb. 16). But his analysis of what to do with the projected budget surplus is not realistic, given the sorry state of Presidential and congressional politicking.

The Democrats and Republicans are bickering over how to spend it. Democrats want more and bigger fiscally irresponsible social programs. Republicans want to reduce taxes by adding back-

door tax breaks and loopholes. I ask: What if congressional gridlock were to continue? We would have a surplus that couldn't be spent. What if the surplus went to paying down our national debt? What if this continued for 20 or 30 years? You see, gridlock is good.

Jeff Varha

Little Canada, Minn.

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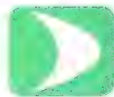
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RIDING THE BULL

My Year in the Madness at Merrill Lynch

By Paul Stiles

Times Business • 323pp • \$25

A FAUSTIAN BARGAIN ON WALL STREET

Sitting in a bar in Princeton, N.J., recently, I overheard a conversation between a young college couple perched nearby. "Goldman Sachs, that's where I want to work," said one, the other nodding in excited agreement. If they only understood what they were wishing for, I thought. Having covered Wall Street for more than a decade, I have often encountered this bright-eyed eagerness among the young. Few understand the price they might have to pay to work at any of the firms in capitalism's engine room: I have seen many of them chewed up and spit out in a heartless and inhumane way. The big money often means big bruises—more, I think, than in other white-collar industries.

That, in a nutshell, is the message of *Riding the Bull: My Year in the Madness at Merrill Lynch*. Unlike Michael Lewis' classic *Liar's Poker* or Frank Partnoy's recent *F.I.A.S.C.O.*, this book makes no claims that Wall Street firms are out to hurt their customers. Instead, it's the employees who get mangled here. The author is Paul Stiles, who spent his 29th year at the New York headquarters of the world's biggest securities firm. A thoughtful young man, Stiles chronicles his journey from earnest supplicant to angry, defeated, and fired ex-goffer. What has he learned? "There is a reason market people are paid so much—the price of a soul is expensive," writes Stiles. "But when looking at the rich, we never think about that. We just want their things."

Stiles begins his tale in Annapolis, Md., where he and his wife were living in the early 1990s. A stint at the National Security Agency had left him disillusioned and feeling it was time to make some money. Why he wanted riches wasn't clear to him—maybe so he could retire at 40, a real possibility for some Wall Streeters. He persuaded his wife to leave their cozy cottage and move to New

York in search of a job. After months of networking with Harvard college friends, placing countless cold calls, and sweating through more than 50 interviews, Stiles landed a junior position at Merrill Lynch & Co.

Unfortunately, his timing was dreadful. It was December, 1993, and the industry was headed into a year of big bond-trading losses. Stiles was in the eye of the storm: He had been hired by the "Latin Mafia" that runs the emerging-markets division of Merrill's massive bond-trading business. Emerging markets, which include the debt of Latin, Asian, and African nations and companies, got slammed in 1994 by Mexico's political upheaval and a sharp interest-rate hike. As for the Latin Mafia—Merrill's incestuous group of Latin American traders and salespeople who specialize in Latin debt—1994's losses marked the end of their clout at Merrill.

Stiles discovered he was as disposable as a piece of furniture. He was absolutely on his own, unable to get any support or guidance from those he had joined. It was a rude awakening for a boy from a close-knit, suburban family.

Rising to the challenge, Stiles clawed his way into several jobs. He describes how he succeeded at one assignment, organizing retail brokers to sell emerging-market bonds. But in time, the infighting and bureaucracy overwhelmed him. A year after he began, sensing that New York had turned him into a greedy, slick, detached person, making money no longer seemed so important. A conversation with his father, a high-school history teacher, about their respective careers proved a turning point. "I realized that a man's moral worth and his net worth were two very different things," writes Stiles. Demoralized and demoted

because of departmental losses, he most courted his own firing. At year's end in 1994, he returned to Annapolis, where he works in marketing.

Riding the Bull provides a worm's-eye view of Merrill Lynch that contrasts with its carefully crafted image of benevolence and intelligence. The firm comes off as a bunch of cowboys who don't hesitate to fire others to keep the bonus pool intact. Stiles's colleagues seem greedy, cowardly, selfish, headless, and not very smart. Moreover, they are abysmal managers: Stiles was shuffled to six separate jobs in his one year of work. And divisional infighting between Merrill's retail brokers and those who serve corporate customers appeared debilitating for everyone.

The experience prompts the author to ponder the source of his obsession with money, something that obviously did not come from his father. He, like many others, had succumbed to the lure of Wall Street without really thinking about why

he wanted to go there. Yet Stiles unconvincingly attempts to shift the blame for his money lust to our society's worship of wealth. "Everywhere where market principles are choking moral principles strip-mining substance, but dozing beauty, razing reason, and we can't even summarize any outrage anymore because we are so deafened by the roar," he writes. Would he have reacted differently had

his timing been better and rewards been greater?

Still, Stiles is a talented writer who can craft a precise metaphor, recreate dialogue, and communicate subtlety and emotion. His is an angry yet gentle protest against being ignored and treated badly. Stiles accepts some blame for his failure. With more perspective, he might realize that he got just what he wanted—and that Merrill was hardly culpable. The firm hired him, an outsider with no connections, and turned him loose. His firing was his own fault: He couldn't overcome his disdain for his employer and, ultimately, for himself. Take note, Princetonians, before you stampede on Wall Street's brutal playing fields.

BY LEAH NATHANS SPIRO

Spiro observes Wall Street's victims and BUSINESS WEEK.



WHY DO BROKERAGE FIRMS PAY SO WELL? "THE PRICE OF A SOUL IS EXPENSIVE"



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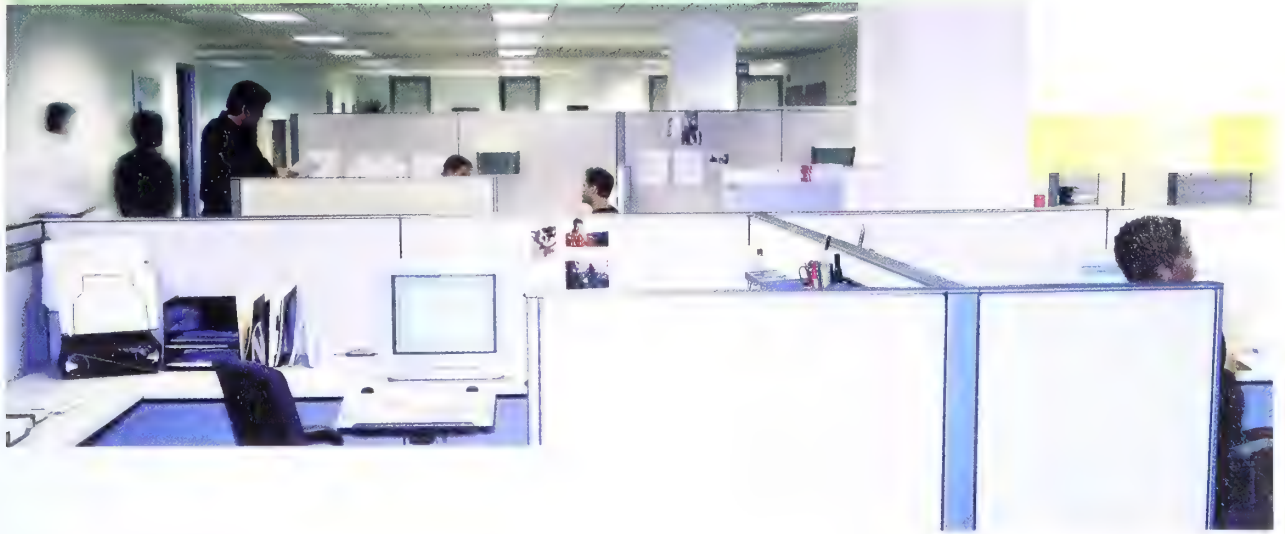
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BY STEPHEN H. WILDSTROM

IS EVERYBODY ON THE SAME PAGE?

If you work on more than one computer, this "briefcase" helps keep them in sync

I'm a three-computer guy. I work on a desktop computer in the office, another at home, and on the road I carry a laptop. I sometimes feel that making sure each machine has up-to-date versions of the data I need is the bane of my existence.

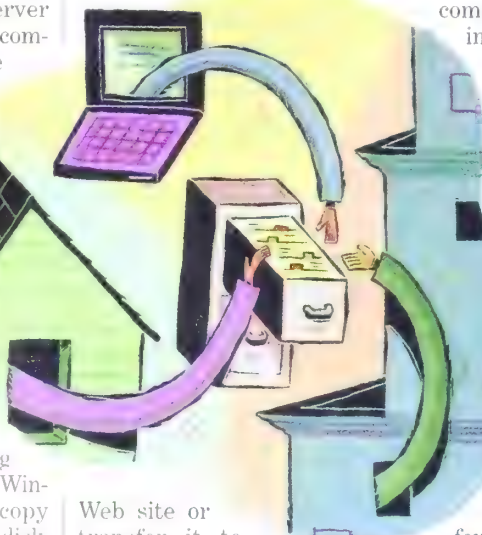
A new Web-based service called Visto Briefcase (www.briefcase.com) promises to ease my pain. It lets you upload files from Windows 95 and NT computers and store them on a server for retrieval from any computer with access to the Web. Briefcase also synchronizes your phone and address book and E-mail inbox, so that once you have read a message on one computer, your others also recognize it as read.

PROBLEMS. The idea behind this has been around for a while. Microsoft put something called My Briefcase in Windows 95. It lets you copy critical files to a floppy disk, then use that disk to synchronize the data with other computers. But there were problems: The software didn't work very well, and a 1.4 megabyte floppy often isn't big enough.

With help from the synchronization experts at Puma Technology, Visto makes the sync software work. And on

the Internet, storage is limited only by the time it takes to do downloads: A Visto account, \$9.95 a month after a 30-day free trial, includes 20 MB of storage.

If you work on more than one computer, I think you'll find Visto as much help as I did. You can synchronize Web bookmarks for either Netscape or Microsoft browsers. The address book takes data from several popular contact managers, including Microsoft Outlook, Symantec Act!, and Starfish Sidekick. Once you have uploaded information, you can view it on your private Visto



Web site or transfer it to other computers. Briefcase does not support calendar synchronization, a serious lack Visto plans to remedy soon.

I found the E-mail clumsy. I could copy messages from a Netscape mail server to my Briefcase, and this will work with most corporate post offices. If you delete a

message from Briefcase, it will disappear from the server the next time you sync. But new messages won't show up in your Briefcase inbox until you sync with the mail server. And reading and managing messages can be painfully slow. If you have the option, you'll probably be better off with direct remote access to your mail system.

SECURITY. Much better is the feature that gives all of your computers access to selected files. You can designate one directory on your computer, say the My Documents folder containing your reports and memos, as the sync folder. Its contents are kept on the Web server. When you sync with another computer, the files are reconciled with the contents of a folder with the same name.

The Visto software allows automatic, scheduled synchronization. But your computer must be logged in at the time, a practice most corporate security policies wisely ban. This can't be fixed in Windows 95, but a coming version of Visto software will take advantage of a feature in Windows NT that lets files be updated without compromising security.

Privacy and security are concerns with any system of this type. Files are encrypted by your browser before transmission and are kept scrambled on the server. This seems adequate for most purposes, but I'd be leery about posting really sensitive data.

I found Visto Briefcase was a big help in easing my multicomputer woes. Anyone who shares my difficulties would do well to give this handy service a try.

BULLETIN BOARD

UPGRADES

A FASTER MAC

Macintosh owners who want the speed of the new PowerPC G3 processor but don't want to buy a new computer should consider the MAXPOWER G3

upgrade cards from Newer Technology (316 943-0222). Unlike most Intel-based PCs, Macs are designed for easy processor upgrades, and the MAXPOWER cards, which range from \$949 to \$2,050, are simple to install. With a G3 upgrade, my PowerCenter Pro 210 from the now-defunct Power Computing outpaced an Apple Power Mac G3 rendering a complex image with MetaCreation's Bryce 3D in 2 minutes 15 seconds, vs. 2:46 for the Mac. The upgrades are likely to be especially popular with graphics pros who want to protect investments in high-end Power Computing PowerTower or Power Mac 9500/9600 boxes. New G3 Macs lack the expansion capacity of the older models.

CELL PHONES

LOOK MA, NO HANDS

Often, it would be convenient to have hands-free use of a cell phone, with driving the leading example. The \$40 EarSet from Jabra (800 327-2230 or 619 622-9955) is a small earpiece that, amazingly, doubles as a good, clear microphone by picking up your voice from the vibrations that speech produces in the bones in your head. The EarSet plugs into the phone's headset jack. A \$40 adapter is required on phones such as analog Motorola flip-phones that lack a built-in jack.

QUESTIONS? COMMENTS? E-mail tech&you@businessweek.com or fax (202) 383-2125

AURA D'ANDREA TYSON

IF THERE WERE NO IMF, THEY'D HAVE TO INVENT ONE



BEHAVIOR?
The fund has played a responsible role in bringing Asia—and the world—back from the brink of a full-fledged collapse

In recent weeks, critics from the right and from the left have launched strident attacks on International Monetary Fund efforts to stem the financial crisis that has swept through Asia like a typhoon. Critics on the right oppose using taxpayers' money to prop up foreign economies that compete with the U.S. They believe that government intervention will mess up the workings of the global financial markets (although the Asian experience reveals that private actors can create quite a mess themselves). Critics on the left see the IMF as the agent of international capitalists, seeking protection from heavy losses caused by their greed and stupidity. They are also outraged by assistance to governments that violate U.S. norms of human rights.

These questions will be hotly debated as Congress considers the Clinton Administration's request for \$18 billion in additional resources for the IMF. But as usual, the political debate threatens to shed more heat than light on the real policy issues. Although the IMF has made mistakes as it struggles with a crisis whose causes and remedies are not fully understood by anyone, it has played a responsible role in bringing Asia, and the world, back from the brink of a full-fledged financial collapse. Examining the facts, not the slogans, is the best way to evaluate the IMF's actions in this crisis and to develop recommendations for improving future policies.

HEFTY RISKS. Without question, the most serious concern about the IMF's intervention is that it contributes to the so-called moral hazard problem, whereby economic actors reap the benefits of their decisions when things go well but are protected when things go poorly. If borrowers and investors do not suffer the costs of bad decisions, won't they be encouraged to make more bad decisions in the future? If the system spares the financial market rod, won't it spoil the financial market child? To some extent, the answer is yes.

Creditors' expectations of being rescued by the IMF may have engendered greater risk-taking than is desirable. But the fact remains that investors and lenders are paying dearly for their behavior. According to Federal Reserve Chairman Alan Greenspan, Asian equity losses outside of Japan have amounted to more than \$700 billion since June, 1997, with additional losses in bonds and real estate. Foreign banks are now car-

rying billions of dollars of bad loans from their Asian activities. Under pressure from the IMF and the U.S., they reluctantly agreed to reschedule South Korea's short-term debt and are negotiating a similar deal with Indonesia. If investors anticipated that they would be largely insulated from the costs of their risky decisions in Asia, they have been sorely disappointed.

LESSER EVIL. A second area of concern is the deflationary effect of the IMF's restrictive monetary and fiscal policy conditions. Won't such conditions cause bank and business failures, trigger a deeper recession, and limit government spending to help the poor? Once again, the answer is yes. But is there a viable alternative? Imagine how foreign investors would have reacted to the IMF advising Asian governments to boost deficit spending and relax monetary policy. The fund prescribed slightly tighter fiscal policy and higher interest rates to stop the free fall of currency values. By the time the Asian economies turned to the IMF, there was little else to do.

Once the panic took hold, prudence dictated that Asian currencies should be allowed to float, at least till confidence in the market was restored. The depreciations of the Asian currencies are not by IMF design. Nor do they reflect market fundamentals. Values have fallen to levels that are understandable only in the context of a sudden shattering of market confidence. Any attempts to support exchange rates during a period of panic are doomed to failure, depleting government reserves and necessitating even bigger infusions of IMF funds. That's why the IMF advised the Asian economies to float their rates, and that's why the IMF strongly opposes the introduction of a currency board in Indonesia at this time.

There is room for improvement in fund practices and policies. The fund must find better ways to bind creditors in, rather than bail them out. And it should do more to fashion its programs to reduce their impact on the poor. But if the world did not have an institution like the IMF to offer temporary financial assistance and technical expertise and to exert multilateral pressure for reform, it would be necessary to invent one. In the meantime, the global economy would run the risk of another contagious financial collapse such as the one in the 1930s that motivated the IMF's creation in the first place.

D'Andrea Tyson is professor of economics and business administration at the University of California at Berkeley and was President Clinton's economic adviser

ROBERT HOLMGRÉN

BY GENE KORETZ

WHAT PUT A DENT IN THE DEFICIT

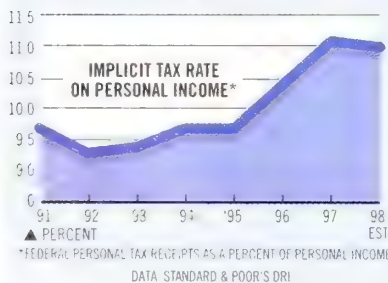
The stock market played a big role

It's amazing how quickly the budgetary debate can change in Washington. A year ago, Congress was projecting a \$124 billion deficit for fiscal 1997 and focusing on how to close the budget gap. A year later, after the deficit came in at a scant \$22 billion, Congress is debating what to do with future surpluses.

Are the politicians jumping the gun? To a large extent, the answer depends on whether last year's startling deficit decline was a one-time fluke or a reflection of persistent new trends.

Economist David A. Wyss of Standard & Poor's DRI, a unit of The McGraw-Hill Cos., which also owns BUSINESS WEEK, is cautiously optimistic.

A LARGER TAX BITE OUT OF INCOME



anticipating "good news on the budget" for some years to come. According to his analysis of last year's budgetary performance, it is the impact of the stock market on revenues that probably holds the key to the positive fiscal outlook.

Wyss attributes about half of the unforeseen \$100 billion decline in the fiscal 1997 deficit to unexpectedly high economic growth and low inflation, a combination that boosted revenues and reduced outlays on social programs. Part also reflected tax receipts on income growth that far exceeded the rise in gross domestic product—a discrepancy that suggests that the economy may have been even stronger than reported.

The real puzzle, however, is the reason for an additional \$50 billion in unexpected personal income-tax receipts—a puzzle that won't be resolved until more precise data are released in a few years' time. It's this revenue windfall

that Wyss attributes to the booming stock market. A clue is the sharp rise in the effective tax rate on personal income (chart), which suggests that the revenues came disproportionately from high-income individuals who have by far the largest stock-market stakes.

To be sure, much of the \$50 billion apparently took the form of taxes on ordinary income rather than capital-gains taxes. But Wyss points out that many capital-gains realizations aren't counted as capital gains. When executives' stock options are exercised, for example, the gap between current market value and their cost is treated as ordinary income. Since high-income execs are taxed at high rates, the current options boom is boosting tax receipts.

Income from 401(k) and IRA plans, which may have big stock holdings, is also treated as ordinary income rather than capital gains. And not only are many retirees now drawing on such plans, but over half of workers who change jobs cash in their 401(k) accounts—thus raising their tax bills.

Finally, Wyss notes that the mutual-fund explosion means that a lot more people now get hit with long- and short-term capital gains each year because of high stock turnover rates. And when the stock market takes off, such gains are inevitably larger, causing an even quicker rise in tax revenues.

If Wyss is right and the recent surge in tax revenues is stock market related, will it continue? Noting that households have accumulated roughly \$3 trillion worth of capital gains in recent years, DRI's economists think the chances are good this year and perhaps for several years more. But the huge stock market gains of recent years cannot last forever. "Over time," says Wyss, "we expect smaller and smaller surprises."

THE PERILS OF STAYING SINGLE

Marriage staves off the grim reaper

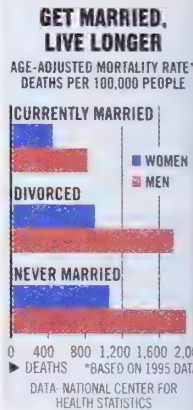
Based on recent U.S. statistics, roughly one out of two marriages these days is likely to end in divorce, and although many divorced people eventually remarry, more Americans than ever are likely to wind up single after marriage or never tie the knot in the first place.

Whatever the social reasons for these trends, their health implications are worrisome. Recent mortality data released by the government indicate that marriage clearly promotes survival. Indeed,

the death rates for currently married men and women are half those of their divorced counterparts of similar ages and less than 45% of those of people who have never gotten hitched.

Even worse than the health prospects of the never married, however, are those of people whose spouses have died. Widowers, in particular, seem to be especially at risk.

Whereas widows' death rates are close to those of women who never married, widowers' rates are significantly higher than those of longtime bachelors.



U.S. WORKERS GET SMARTER

Experience and schooling pay off

Has U.S. productivity entered a higher growth path? True believers argue that business' huge investment in computer technology is finally paying off, and they point to the latest surge in productivity—growing by almost 2% for two years in a row—as evidence.

Most experts remain skeptical, however, claiming that productivity surges for a year or two don't constitute a trend. Still, economist David H. Resler of Nomura Securities International Inc. notes that qualitative changes in the workforce, as well as in technology, argue for a productivity pickup.

Specifically, Resler observes that the average age of the workforce continues to rise, approaching 38.8 years for men and 38.5 years for women. If increasing age reflects increasing average "experience," he says, male workers now have seven months and female workers four months more experience than they had just three years ago.

Resler also notes that college graduates account for nearly 60% of labor force growth and over half of the new jobs created since 1994. Thus, not only the experience level but the educational attainment of the workforce has been rising. The upshot is that greater investment in "human capital" has paralleled growing investment in fixed capital. "A higher trend in productivity growth," says Resler, "should surprise no one."

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DEAN WITTER

GROWTH BECOMES SUBDUED, D WILL THE FED

Greenspan tells Congress he's wary of the economy's momentum

U.S. ECONOMY

Federal Reserve Board Chairman Alan Greenspan's semi-annual defense of monetary policy in front of Congress will not be as easy as it gets. Given the economy's exemplary performance in 1997, the only testimony Greenspan was to say that the economy grew 3.9%, inflation fell to 1.9%, the unemployment rate fell below 5% and the Fed barely had to raise interest rates.

That's pretty much the way it went as financial markets around the world tuned in to Greenspan's Feb. 24 Humphrey-Hawkins testimony on Fed policy and the economy before the House of Representatives and the Senate. In addition, the chairman discussed the reasoning behind last year's policy decisions and laid out the Fed's economic forecast for 1998 (table). Taken all together, his remarks go a long way toward revealing that 1998 policy is likely to evolve.

A FED'S-EYE VIEW OF THE ECONOMY

THE FEDERAL RESERVE'S CENTRAL TENDENCY FORECAST

	1997 ACTUAL	1998 FORECAST
GDP*	3.9%	2.00-2.75%
UNEMPLOYMENT*	1.9	1.75-2.25
INTEREST RATE	4.7	ABOUT 4.75

DATA: FEDERAL RESERVE, BUSINESS WEEK

strength in domestic spending and tightening labor markets." That's Fed-speak for, "If Asia doesn't slow the economy, we're going to have to."

In fact, February data on soaring consumer confidence, robust retail activity, and lower unemployment rates show that domestic demand and the labor markets are as strong as ever. And lower energy prices are helping the Labor Dept.'s revamped consumer price index line, a trend that adds to workers' buying power.

NEVER, GREENSPAN ALSO SAID the outlook satisfies the expectation that any inflationary effects of tight labor markets will largely be offset by "healthy productivity growth, flat or declining import prices, little pressure in commodity markets," along with technical adjustments to the CPI. If all those assumptions are borne out, there will be little reason for the Fed to do anything for the rest of the year. Rapid productivity gains continue to play a promi-

nent role in Greenspan's thinking—and in policy decisions. In fact, he said the pickup in productivity growth in recent years is probably greater than can be explained by usual business cycle forces. Greenspan is clearly suggesting that the economy may be close to a new threshold of noninflationary economic growth.

Faster productivity growth was one of four reasons Greenspan offered for why, despite continued tightening in the labor markets, the central bank did not lift interest rates in 1997 after its quarter-point nudge in March. The other explanations were the appreciation in the dollar, weaker commodity prices, and a passive tightening that resulted when real short-term interest rates were pushed up by falling inflation. Greenspan said higher real rates were "by no means inadvertent."

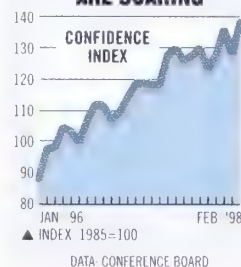
UNLIKE MANY OF his murkier Fed speeches, Greenspan's talk this time was very clear on his concern about the future strength of domestic demand—and with good reason. The latest data show that consumer fundamentals remain solid, and households are responding by increasing their spending further.

In particular, consumers are the most optimistic they have been in a generation, according to the Conference Board. The board's index of consumer confidence jumped 10 points, to 138.3, in February, the highest reading since October, 1968 (chart). The part of the index that covers consumers' current economic situations surged from 159.3 in January to 172.5, while expectations for the future rose from 107.7 to 115.6. A rosy job outlook seems to be more important to consumers than any foreign dilemmas or domestic political scandal, said the board.

The healthy job market and low inflation are boosting household buying power. Real earnings rose 0.9% in January, 3.4% above their year-ago level. Income growth was one factor that Greenspan pointed to when he said that "domestic demand retained considerable momentum at the outset of this year." And that claim was supported by weekly store surveys that show retail sales are up strongly in the first three weeks of February.

For now, at least, the Fed's forecast partly depends on a widening trade deficit to neutralize the might of

CONSUMER SPIRITS ARE SOARING



Business Outlook

domestic demand. That may be already happening. The trade gap worsened by an unexpectedly large amount in December, when the deficit rose to \$10.8 billion, from \$8.7 billion in November. Although December exports rose a respectable 1.3%, imports surged 3.6% to another record of \$90.8 billion.

The larger-than-expected December deficit means that economic growth last quarter was less than the 4.3% rate originally reported. The drag from trade will continue in 1998. Signs of weaker export demand from Asia are starting to show up, and the dollar's strength will continue to push down import prices.

CHEAPER IMPORTS, HOWEVER, are a big reason that Greenspan sounded optimistic about the inflation outlook. CPI revisions are another consideration. Greenspan acknowledged that "technical adjustments [will shave] a couple tenths from the published CPI." Such adjustments, which are ongoing at the Labor Dept., already have trimmed about three-tenths of a point from annual inflation since 1995.

Starting with the January release of the CPI, which showed no change in the prices of goods and services, the Labor Dept. has reorganized the categories in the index and refigured their weights, using consumer surveys of spending habits from 1993 to 1995 that replace buying trends from 1982 to 1984 (table). One big revision was an explicit weighting given to com-

puters, which previously were lumped into a broad category. Computers and related equipment make up less than 1% of spending, but their prices have dropped 13.6% over the past year. Further price declines will offset increases in other prices.

Those increases are most likely to come in service prices. "Providers of services appeared to be more pressed by mounting strains in labor markets," said the chairman. And rising labor costs may force some service companies to raise prices. Also, the robust housing market is beginning to lift housing costs and rents, and shelter has the biggest weight in the CPI.

In discussing the outlook, Greenspan noted that the unknown effects of the Asian crisis meant that the Fed forecasts "are more tentative than usual." But while the chairman noted significant risks on both sides of the outlook, he appeared to be more concerned about a stronger-than-expected economy. And if the data remain as powerful as they have been recently, that concern may well be justified.

SO THIS IS WHERE ALL THE MONEY GOES

SPENDING WEIGHTS FOR THE CPI

	OLD	NEW
FOOD AND BEVERAGES	17.5%	16.3%
HOUSING	41.5	39.6
APPAREL	5.3	4.9
TRANSPORTATION	16.6	17.6
MEDICAL CARE	7.4	5.6
RECREATION/1	4.3	6.2
EDUCATION & COMMUNICATION/2	NA	5.5
OTHER GOODS & SERVICES	7.4	4.3

1/FORMERLY ENTERTAINMENT
2/NEW CATEGORY DATA: LABOR DEPT.

BRAZIL

THE STORM BEFORE THE CALM

Brazil faces some tough going in coming months, but barring any more shock waves from Asia, the economy appears set to recover in the second half with its currency intact.

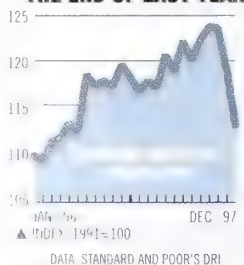
The Asian crisis hit Brazil hard as speculators attacked its currency, the real. So far, the real has survived but at great cost to the economy: The government doubled interest rates, to 40%, and enacted fiscal austerity measures equal to nearly 2% of gross domestic product. These moves prevented a potentially disastrous outflow of foreign capital needed to finance Brazil's fiscal deficit, nearly 6% of GDP, and its current-account deficit, 4.2% of GDP.

Signs that Brazil is slipping into recession are already showing up. Industrial production in November and December plunged 3.5% and 5%, respectively, led by credit-sensitive sectors such as autos, appliances, and capital

goods (chart). Unemployment is rising, with January joblessness in São Paulo at 16.6%, up from 13.9% a year ago. Credit delinquencies are increasing, suggesting further weakness in consumer spending that will force more

production cutbacks in coming months. Fourth-quarter real GDP grew 0.5%, bringing 1997 growth to 3%. With the GDP expected to fall in the first half, 1998 growth is projected at 1%.

OUTPUT PLUMMETED AT THE END OF LAST YEAR



But some key problems are abating. Slower economic growth is already narrowing the trade deficit as imports fall, and analysts expect a trade surplus by midyear. Also, social security and administrative reforms moved forward in Congress in February, with final approval possible in March.

Most important, foreign capital is flowing in despite recent interest-rate cuts, including a big one on Jan. 29 that lowered the prime rate from 38% to 34.5%. Foreign exchange reserves rose to \$58 billion by late February from \$52.5 billion at the end of January, and foreign direct investment, which rose \$924 million in January, had gained \$717 million more by mid-February. Assuming Asia remains calm, Brazil is set to cut rates further, bolstering the outlook for a recovery in the second half.

Vantive Passes Siebel

From a cold start — a little more than a year ago — Vantive now outstrips Siebel in the number of new customers choosing our sales force automation product every quarter. This is rather unusual, and begs the question, "What happened?"

Perhaps it started with our roots in the customer-satisfaction business. But it clearly ends with things as simple as our *open-book* reference policy, our rapid 6-second on-average field-sales-rep synchronization (versus ... well ... just ask Siebel), and our 550-customer dominance in the front office.

If you're considering sales, marketing, customer service or field service application software from *anyone* else, we invite you to call for the free *ROI for Mere Mortals* bible. Or visit our Web site. While you still have a prayer. Selah.



Vantive.
Because Customers
Are Your Most Valuable Asset™

Call 1-800-VANTIVE

(1-800-820-8485 or 1-877-257-001 from outside the U.S.)

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TWO REASONS NOT T

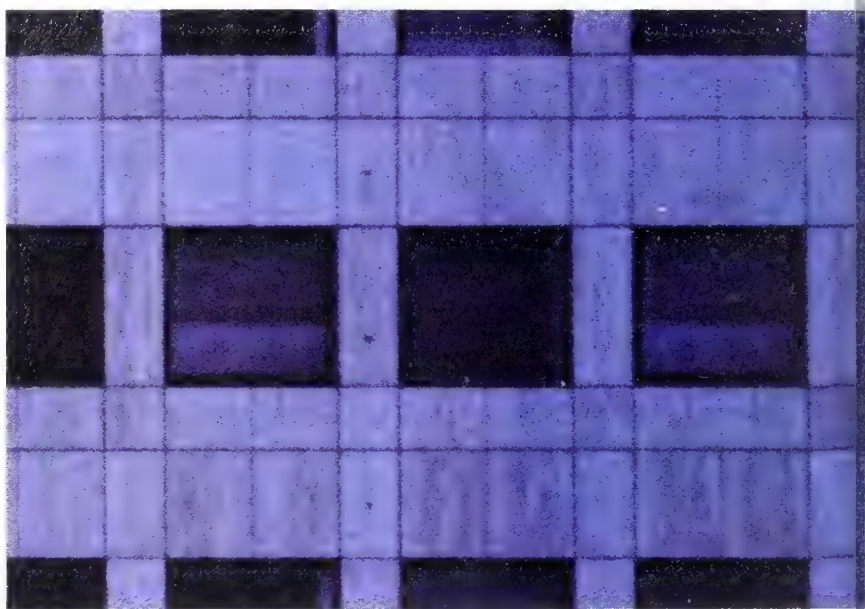
When Federal Reserve Board Chairman Alan Greenspan laid out for Congress the Fed's forecast for the economy on Feb. 24-25, he stressed two key areas: productivity and foreign trade. Why? Because both could have a major impact on how the economy and monetary policy unfold in 1998.

In the past, the current mix of strong domestic demand and tight labor markets would have set off inflation alarms. But Greenspan & Co. are betting that 1998 will be different. That's because the Fed's forecast of moderating economic growth and continued low inflation is founded on the belief that productivity gains will continue to offset rising labor costs and that the Asian crisis will widen the U.S. trade gap, helping to slow the economy and relieve inflation pressures.

But will it work out that way? BUSINESS WEEK reports that U.S. companies believe the Fed chief is right on the money. Businesses continue to squeeze efficiencies from their operations by various means, including continuing investment in new technologies. And with pricing power weak, rising labor costs only add an incentive to boost productivity further.

Moreover, the widening trade deficit now may no longer cause severe dislocations. True, imports are rising rapidly and will continue to do so. But some 40% of those foreign goods now originate from U.S. foreign affiliates, and many imports are capital goods, which increase productivity.

Here is BUSINESS WEEK's assessment of how the two critical forces will be felt in 1998.



THE PROMISE OF PRODUCTIVITY

It's getting tougher, but companies keep finding ways to squeeze more out of their operations

If you find yourself working harder, glued to your computer, don't take it too hard. In fact, you can give yourself a nice big pat on the back, because you're part of the productivity boom that Federal Reserve Chairman Alan Greenspan is counting on to keep the U.S. economy humming—without overheating.

Continued productivity gains are critical to maintaining a delicate balance between growth and inflation, and so far, things are looking good. Nonfarm productivity has increased 2% on average over the past two years, and man-

ufacturing productivity increased 4.4% in 1997 alone.

All across America, executives and managers are burning the midnight oil to figure out how to wring further gains from their businesses. The challenges are getting bigger: With unemployment at a quarter-century low of 4.7%, wages are on the rise. Hourly compensation rose at a 4.9% annual pace in the fourth quarter of last year, and the minimum wage jumped from \$4.25 to \$5.15 an hour. Yet companies can't raise prices to offset their rising labor costs: The consumer price index is up a mere 1.6% over the past year, and the core producer price index is down slightly over the same period. With a tidal wave of low-cost imports washing up on American shores (page 30), the squeeze will only worsen.

The basic tactics are well-known now: downsize, restructure, consolidate, tie compensation to company profits.

NKER



invest huge sums in high-tech equipment. But this time around, with inflation giving managers little room to maneuver, the push is on to do more with less and strive for even greater gains in efficiency. "We are obsessive about productivity," declares Daniel G. Arnham, vice-chairman of Allied Signal Inc.

It's a sentiment that Greenspan expresses—in his unique Fedese. "The impact of rising costs in tight labor markets has imparted a substantial impetus to efforts to take advantage of available efficiencies," Greenspan said in testimony before Congress on Feb. 24.

Witness the renewed emphasis on cost-cutting. In the fourth quarter, U.S. companies announced plans to eliminate 152,854 jobs, up 33% from the same period in 1996, according to Challenger, Gray & Christmas Inc., the international outplacement firm. The carnage continues. On Feb. 24, First Union Corp. announced it would eliminate 4,400 jobs as it digests its latest acquisition, Corestates Financial Corp.

Companies continue to shift manufacturing offshore, too. On Jan. 28, Phillips-Van Heusen Corp. closed down its G. H. Bass plant in Wilton, Me., and moved operations to Puerto Rico. In Maine employee pay averaged \$9 an

hour—a hefty premium over what Puerto Rican workers earn.

With an eye toward productivity gains, Corporate America continues to invest heavily in technology. From 1990 to 1996, companies spent more than \$1.1 trillion on information-technology hardware alone, according to Stephen Roach, chief economist at Morgan Stanley, Dean Witter, Discover & Co. That spending should increase: A poll by the Federal Reserve Bank of Minneapolis in its region found that 45% of respondents planned on hiking capital spending this year, while only 26% said they would increase full-time employment. Says Sung Won Sohn, chief economist at Norwest Corp.: "The answer to labor shortages is to employ more modern technology."

THINKING SMARTER. St. Paul Cos., the giant insurer based in St. Paul, Minn., certainly agrees. It is aiming for productivity growth rates of 5% annually over the next several years, more than enough to cover its expected increase in labor costs, says Patrick A. Thiele, head of the company's worldwide insurance operations. One way to reach its goal is to increase info-tech spending some 10% to 15% a year. "We are continually replacing human capital with information-technology capital," says Healy.

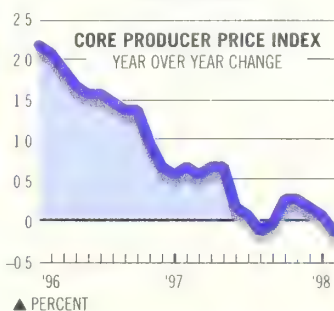
Similarly, Howard Schultz & Associates of Dallas, an accounts-payable auditing firm, says it recovered more than \$560 million in accounts-payable losses last year, up 32% over '96—and with the same number of people. Thanks to improvements in the information systems used by its customers and better

WORKING
HARDER
FOR THE
MONEY

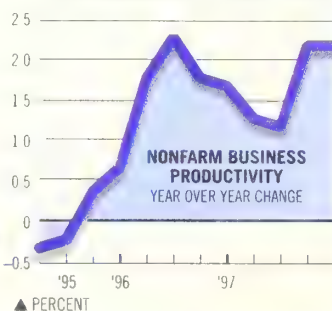
WITH LABOR COSTS RISING...



...AND PRICES FALLING...



...COMPANIES PUSH FOR GREATER PRODUCTIVITY



software developed in-house, the company can do more work without adding employees. "We're in a position where we can do more and do it faster," says CEO Howard H. Schultz.

Sometimes, boosting productivity simply means thinking a little smarter. Take Southland Corp., the Dallas-based parent of the 7-Eleven convenience-store chain. Southland figures pay for store employees rose 4.8% in 1997. "The increase in the minimum wage combined with the tight labor markets is really sneaking up on people," says Rick Updyke, manager of planning at Southland. So Southland has developed a worksheet for store managers that helps them match such tasks as stocking shelves to employees' hours worked. Southland is far from alone. Says Mitchell S. Fromstein, chairman of Manpower Inc., the giant temporary-help provider: "Major companies are beginning to look just as much at the cost of labor downtime as machine downtime."

DROPPED SALADS. When squeezed between rising costs and a zero-inflation market, some companies must make tough choices. Anticipating Oregon's minimum wage hike to \$6 an hour in January, Burger King Corp. franchisee Jack Eberly dropped prepared salads from the menus of his 11 restaurants in Eugene. The change let his restaurants operate with one less person in the morning shift because it cuts prep time.

Another factor in the productivity equation is training. Take AlliedSignal. The \$14.5 billion industrial behemoth has an ongoing goal of achieving annual productivity gains of 6% a year by using what it calls the "Six Sigma" manufacturing quality program. Under Six Sigma, Allied is out to get defects down to 3.4 per million products coming off the assembly line. About 6,000 employees have already been trained in the program, and this year another 2,000 workers will be taught to apply Six Sigma in other areas. The bottom line: Fewer mistakes from beginning to end means better output per employee.

There is no question that companies face enormous profit pressures. Yet throughout the 1990s, economists have underestimated the ability of managers and workers to boost productivity by investing in high-tech equipment and restructuring the workplace. There's no sign of a letup. That's good news indeed for the economy. So, do your part.

By Christopher Farrell in St. Paul, with Amy Barrett in Philadelphia, Gail DeGeorge in Miami, Wendy Zellner in Dallas, and bureau reports

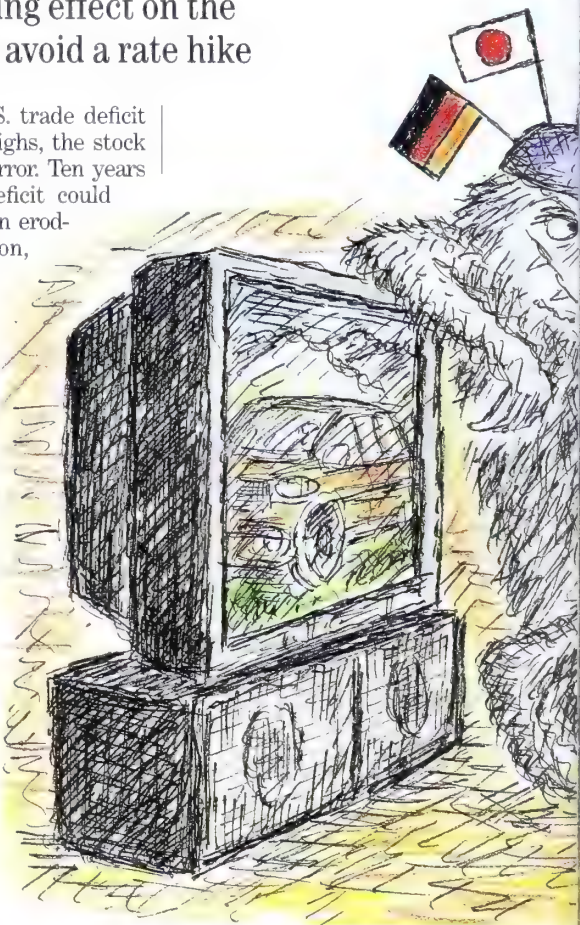
THIS TRADE DEFICIT COULD HELP

It may have a cooling effect on the economy and help avoid a rate hike

The last time the U.S. trade deficit was setting record highs, the stock market recoiled in horror. Ten years ago, the swelling deficit could mean only trouble ahead: an eroding dollar, rising inflation, soaring interest rates, and displaced workers. The rising deficit and the spike in interest rates that followed brought down the market in October of 1987.

And now? On Feb. 19, the Commerce Dept. reported a record \$199 billion merchandise trade deficit for 1997. Economists warned that the gap could widen to as much as \$300 billion in 1999. The market reaction: The Dow closed out the week just off an all-time high and on Feb. 25 set a new record: 8458.

Yes, a skyrocketing trade deficit still matters. But there are good reasons not to sound the alarm this time. For one thing, more comprehensive measures of the deficit are not setting records. More important, the deficit isn't actually that big: It's just 1.2% of gross domestic product, compared with 3.0% in 1987. (chart). **CONFIDENT CONSUMERS.** Indeed, today's trade picture reflects a sign of the robust American economy. U.S. exports keep growing despite a strong dollar. Meanwhile, consumers confident of their earning power in an economy with 4.7% unemployment are stocking up on imported cars, electronics, and wine—without fear of putting their fellow Americans out of a job.



And with the U.S. budget finally in balance, there's also no problem luring foreign capital. "In the 1980s, the trade deficit was a fundamental reflection of a sick U.S. economy with very low investment and savings and a huge budget deficit," says Boston College economist Alicia H. Munnell. "Now, the gap reflects the strength of an economy that's attracting very high investment."

Part of that strength comes from the way U.S. multinationals have changed their M.O. over the past decade. Instead of simply shipping U.S.-made products to overseas markets, they have dispersed

Today's gap isn't actually that big,

action to foreign outposts to cut and serve those markets better. The moves, plus currency hedging, cushioned the effect of regional turns.

It's not to say that an exploding deficit doesn't pose danger. A surge in exports from Asia could shave up to a percentage point off GDP growth, giving a 2%-to-2.75% rise this year; most economists expect. Federal Reserve man Alan Greenspan welcomed the effect on the fast-growing economy, but warned that "storm clouds" over will hold down exports.

And there are limits beyond which deficit can't go without taking down the dollar and undermining the whole economy. Currency traders still hit the switch when they see a nation's current-account deficit—the total mea-

despite Asia, the export picture still looks promising. Canada and Mexico—the No. 1 and No. 2 export markets—are expected to post 1998 growth rates of 4% to 6%. For many exporters, European sales also remain strong. Take Microsoft Corp. Its Asian sales fell 8% last quarter, and it warned of increased softness to come. But the drop was more than offset by a 33% increase in sales to Europe. That helped the company post a 34% revenue gain last year.

Still more significant: the global reach so many companies have attained. Levi Strauss & Co.'s "proximity to market" strategy has put it in 60 countries. "For a global company such as ours, this U.S. trade deficit is a wash," says Clarence Grebey, director of global communications. Alan F. Shugart, CEO of disk-drive maker Seagate Technology Inc., agrees:

totalled \$461 billion—\$85 billion in '97 alone. The U.S. now accounts for a quarter of the world's total foreign direct investment and 40% more than Germany and Japan combined.

Another change: These days the multinationals travel in packs. "We trade pretty much globally, typically with global companies that can move with us" by shifting orders to any given locale, says Carl E. Snyder, head of procurement for Hewlett-Packard Co.

UNHAPPY CARMAKERS. The upshot: An astonishing 40% of imports to the U.S. now originate from U.S. affiliates abroad, meaning that much of the profits wind up back in the U.S. anyway, supporting the higher-paid engineers, research scientists, and managers. "Even if imports overwhelm exports in the near term, foreign investment keeps our export boom going,

helps maintain our global competitiveness, and supports employment here," says Joseph P. Quinlan, a trade economist at Morgan Stanley, Dean Witter, Discover & Co.

Not everyone is happy. Take Detroit's car-makers, struggling with Asia's protected industry. Since General Motors Corp.'s Saturn division began selling its small cars in Japan last year, the yen fell against the dollar, costing Saturn \$4,000 per vehicle. Result: Saturn runs deep in the red there.

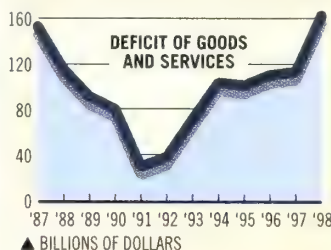
Still, most U.S. multinationals are far more confident about facing down Asian rivals than they were 10 years ago. "In the long term, the Asian turmoil will actually hasten the opening of markets and allow the

free-market system to determine who wins," predicts Joseph T. Gorman, CEO of Cleveland-based TRW Inc., global supplier of air bags and other auto parts. GM CEO and Chairman John F. Smith Jr. agrees: "The best thing for us is to work like the devil to be able to compete aggressively in the market." As long as the rest of the U.S. economy remains on solid ground, the trade deficit is likely to elicit more yawns than yelps.

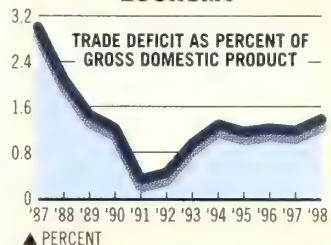
By Paul Magnusson in Washington, Thane Peterson in Frankfurt, Katie Kerwin in Detroit, Peter Burrows in San Mateo, and bureau reports



THE TRADE DEFICIT MAY BE GROWING AGAIN...



...BUT SO IS THE ECONOMY



DATA: CENSUS BUREAU, BUREAU OF ECONOMIC ANALYSIS

of trade in goods, services, and investment flows—approaching 3% of GDP. As investors might then fear a collapse. They would pull their money out of the U.S., forcing the greenback down further and potentially reigniting inflationary pressures—prompting the Fed to raise interest rates. On the 25th, Greenspan noted that for the dollar, there is no near-term problem." But, Goldman Sachs economist Thomas H. Lee said: "The rising U.S. current-account deficit could be the Achilles' heel of the dollar."

But the deficit isn't out of control. And

"There's two sides to the Asia situation. If you're selling there, you'll sell less because the companies there have less to spend. But we can build over there for a lot less. And boy, the cost of doing business over there has dropped. For us, it's more of a positive than a negative."

U.S.-owned plants abroad have actually been far more critical to the U.S. global expansion than rising exports. U.S. industry now earns more than three times as much from sales by foreign affiliates than from export sales originating at U.S. plants. Foreign direct investment by U.S. companies since 1990 has

sign of a robust economy luring lots of foreign capital

TELECOMMUNICATIONS

WIRELESS GOES HAYWIRE
AT MOTOROLA

Faulty switches, a tarnished reputation—how bad can it get?

Wireless technology is supposed to be Motorola Inc.'s strong suit. But lately the deck seems to be stacked against the electronics giant. Upstarts have beaten it to market—by years—with new digital phones. And its transmission equipment for digital-cellular networks has been plagued by bugs. With its once-indomitable paging business shrinking and formidable competition squeezing its semiconductor division, it's unclear what sector the \$30 billion company can depend on for growth. Wails one Motorola executive: "It's the freaking Titanic over here."

And there's an iceberg ahead. By early March, PrimeCo Personal Communications—a wireless service owned by Bell Atlantic, U S West and AirTouch Communications—is expected to cancel a \$500 million contract with Motorola for digital network equipment. Rival Lucent Technologies Inc. is expect-

ed to get the business, one of the biggest orders in the industry. "To replace a half-billion dollars? Ouch," says telecom analyst Ian Gillott at International Data Corp.

How bad will it hurt? Even before the anticipated loss of PrimeCo, Furman Selz Inc. has already slashed its Motorola 1998 earnings estimate to \$2.38 a share from \$2.80 and its 1999 estimate to \$2.80 a share from \$3.80. "The rest of the business is experiencing worse-than-expected performance," says analyst Susan Kalla.

The misfires raise questions about how Motorola, longtime leader in analog-wireless systems, will fare as the industry moves squarely into the digital age. Last summer, faulty base station regulators that direct calls interrupted service on PrimeCo's digital network in Chicago. The network—using so-called CDMA code—typically stayed down from 30 minutes to two hours because Motorola didn't have enough engineers to fix the problem, executives close to the company say. Though it accepts responsibility for the outages, a top Motorola executive disclaimed: "Rarely is software perfect the day it's rolled out."

For Motorola, this is particularly true. It had software problems with equipment it supplied GTE Wireless and Nextel Communications Inc., too. But those companies say they will stick with Motorola. "With any vendor, you run into occasional problems," says

John McLean, GTE Wireless' vice-president of technology.

Motorola has been scrambling to bring its digital portfolio up to speed. An aggressive pitch to Sprint PCS last spring landed the company 60% of a \$750 million contract to complete the construction of Sprint's digital network. And on Feb. 1 at the Cellular Telecommunications Industry Assn. convention in Atlanta, Motorola announced its first commercial availability of CDMA digital phones.

CATCH-UP. Still, Motorola is playing catch-up. Qualcomm Inc., for example, has already released tiny CDMA phones the size of cigarette packs. Motorola

isn't expected to have a digital version of its compact StarTac phone until the end of this year.

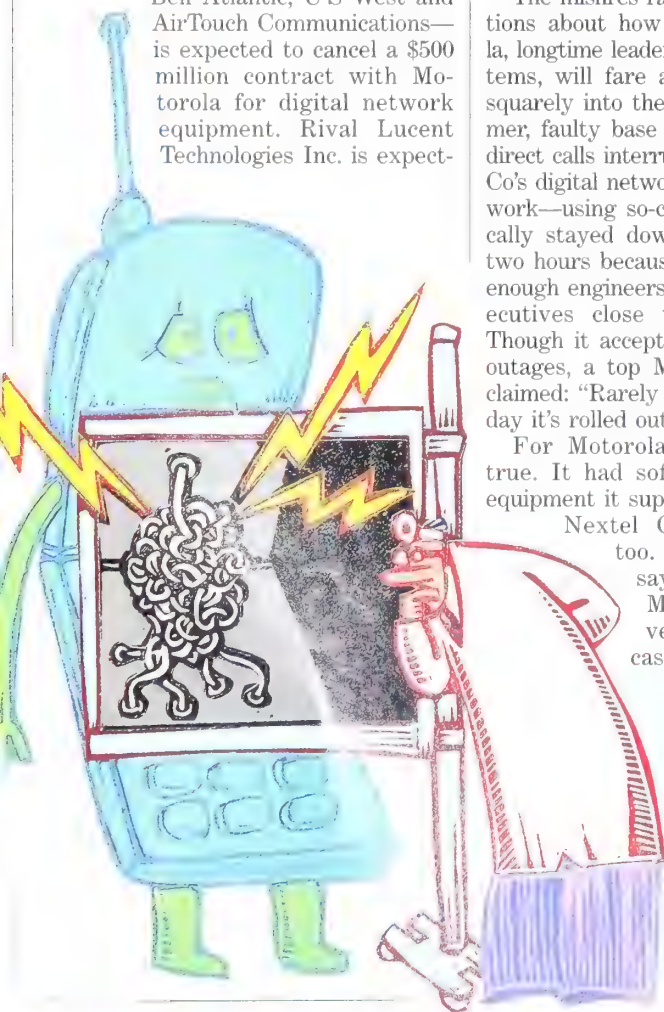
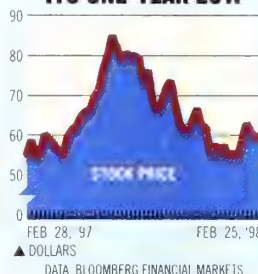
The lack of competitive phones is quickly leading to lost market share. AT&T Wireless says its new subscribers are choosing digital as much as 85% of the time—because they're cheaper to use, have longer battery life, and more easily accommodate

features like E-mail.

Motorola also faces quality questions with its digital phones. Recently, the company had to issue a software upgrade for digital phones in Latin America because the handsets shut down when they received unfamiliar signals from network equipment. BellSouth, SBC Communications, and AT&T Wireless have chosen other than Motorola technology. A BellSouth spokesman says the company would like to have a digital Motorola product in its mix, but none has passed its "shake and bake test."

"Their brand has eroded," adds Gary Cuccio, COO at Omnipoint Communications, an East Coast digital phone carrier. While some customers still accept Motorola gear, "it's not like they have the products." How times have changed.

By Roger O. Crockett in Chicago and Peter Elstrom in New York and Gary McWilliams in Houston

MOTOROLA IS NEARING
ITS ONE-YEAR LOW

UNTANGLING THE WIRELESS MESS

IMPROVE reliability of digital "infrastructure" products.

RECOVER lost market share in digital phones—where Motorola is two years behind in shipping popular CDMA phones.

REBUILD relations with customers. Many carriers and distributors complain that Motorola's arrogant style has turned them off.

**If a tree falls on your car
in the forest,
does anyone hear it?**

hits tree. Or tree hits car. Airbags inflate. OnStar Center is
ed. Computer map pinpoints location. Advisor calls back,
no answer. Advisor calls nearest emergency service provider.
someone will hear you. 24 hours a day, 7 days a week. Even
u can't call, we'll hear you. We'll hear you in other ways, too.
u're lost, we'll direct you. If your car is stolen, we can track it.

If you're locked out, we can unlock. It's a service called
OnStar. It's available on nearly 2 million new GM vehicles.
And it gives you more peace of mind. Because it's a jungle
out there. Even when it's only a forest. For
more information, call 1-888-ONSTAR-7
or visit our website at www.onstar.com.





DEALS

JOHN AND MIKE'S BIG ADVENTURE

A TCI-AT&T connection may come to pass—but can it work?

In January, as he made his first major presentation to Wall Street analysts, AT&T CEO C. Michael Armstrong found himself violating the company's policy of not commenting on possible deals. The reason? The market buzz about a merger with Tele-Communications Inc. (TCI) had become a roar. "We won't be announcing a cable acquisition at the end of the meeting or in the near future," he told the crowd.

Well, maybe not an acquisition. But more deals between Armstrong and TCI's CEO John C. Malone seem about to hatch. The two execs are negotiating a pair of investments that would bind the two companies more closely together and give AT&T a critically important path to enter the \$100 billion local phone market. AT&T is discussing a \$1 billion-plus investment in @Home Corp. in exchange for an equity stake in the high-speed Internet access provider, whose largest shareholder is cable giant TCI.

On Feb. 20, @Home confirmed the AT&T talks, sending its shares soaring. AT&T would market the @Home service to its customers, and it would probably

fold its WorldNet Internet service's 1.1 million subscribers into @Home. According to one AT&T source, the giant is looking to get a 20% @Home stake—as large as TCI's—so that it will have an equal say in management.

AT&T is after more than fast Internet links. What AT&T hopes for is a means to end-run the Baby Bells and provide local phone service over the cable network. That would not only save \$16 billion in access charges AT&T pays local carriers annually but also give it control over its service. To that end, AT&T is discussing a separate investment in TCI that could reach \$1 billion. That could be a flat equity investment—or the phone company may chip in \$100 for every set-top box when TCI starts deploying telephone-capable boxes in 1999.

While a TCI investment could come by mid-March, the @Home deal may take longer. @Home is talking about merging with the Net access businesses of Time Warner Inc. and U S West Media Group. Since that would make @Home more attractive to AT&T, Malone wants the deal cut before moving

forward. TCI, however, is motivated to make a phone deal. Malone regards Internet telephony as one of his most promising avenues for growth. Neither AT&T nor TCI would comment on negotiations.

Even if Armstrong and the notoriously tough Malone come to terms, cable telephony is far from a sure bet. They need to agree on who will invest the billions needed

to upgrade the cable network for voice and how to divvy up calling revenues. Even then, AT&T could end up with poor-quality service that would hurt its reputation. The Internet technology that AT&T and TCI plan to use has proved problematic, and what more, cable networks are so far not as reliable as phone systems. "If they're trying to use this as a bridge to the local customer, it's a very weak bridge," says Scott C. Cleland, an analyst at Legg Mason Inc.'s Precursor Group.

LITTERED PATH. Armstrong may have to chance the crossing. AT&T's acquisition of Teleport Communications Group, an "alternate access company" partly owned by TCI and other cable companies, gives it an entrée into the \$20 billion local business market. But Armstrong still needs an economical way into the \$80 billion residential market before the Baby Bells start offering long-distance service. Potentially, cable telephony gives AT&T what it needs to match the new competition with a local and long-distance bundle.

Still, more cable-telco deals have been drawn up than carried out. In 1995, Malone agreed to merge with Bell Atlantic Corp. That fell apart two years later, when Bell Atlantic went sour on cable. In 1996, Sprint Corp. had big plans to provide local phone service over the cable network. That prospect died because the costs were prohibitive. "What does AT&T know that Sprint didn't know?" says Cleland. Another question for Mr. Armstrong.

By Peter Elstrom in New York and Ronald Grover in Kansas City, Mo.

AT&T'S COURTSHIP OF CABLE

DIRECTV In December, AT&T sold its 2.5% stake in the satellite television business back to Hughes Electronics. Cable companies had felt threatened by DirectTV.

TELEPORT COMMUNICATIONS GROUP In January, AT&T agreed to acquire TCG for \$11.3 billion. That gave TCG's owners, including TCI, a 10% stake in AT&T.

@HOME AT&T is negotiating to take an equity stake in the high-speed Internet access provider. It's likely to invest at least \$1 billion and receive a stake equal to TCI's holding.

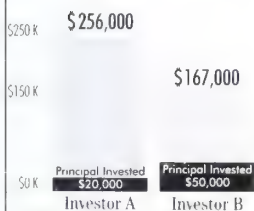
TELE-COMMUNICATIONS AT&T is also negotiating to take a stake in TCI, in part so that the two can cooperate on cable telephony. The investment could total \$1 billion.

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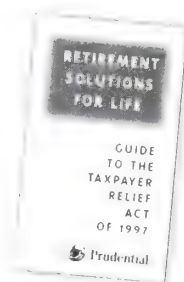
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COMPUTERS

THE GREAT



DEBATE

Congress is getting nowhere in the battle to control encryption

For years, the battle over data encryption—the technology used to keep computerized information confidential—was an arcane fight over export controls. National Security Agency spooks wanted tight controls to keep software capable of cloaking information with an unbreakable code out of the hands of terrorists. U.S. industry protested that such restrictions would cut off billions in sales and curtail the growth of electronic commerce—without doing much to boost national security.

Then last year, the debate took a dramatic and, some would argue, dangerous turn. FBI director Louis J. Freeh called for domestic controls on encryption, as well. Without them, he argued, law enforcement agencies would be hamstrung. Key members of Congress agreed. Last September, the House Permanent Select Committee on Intelligence gutted an industry-backed bill to relax export controls and replaced it with a measure that would prevent anyone from making, distributing, or selling any encryption product that didn't provide "keys" to unlock coded information that police could seize. Privacy advocates on both sides of the political spectrum were aghast. Companies, who want to assure consumers that doing business on the Net is completely secure and confidential, foresaw lost billions.

"STALKING HORSE." Now, opponents are mounting a counteroffensive. Organizations such as Microsoft Corp., the U.S. Chamber of Commerce, and the Business Software Alliance plan to contribute more than \$10 million to finance a massive lobbying and publicity campaign to beat back domestic controls and relax export restrictions. Heading the offensive are Washington insiders Edward W. Gillespie, who helped write the GOP's Contract With America, and Jack Quinn, former chief of staff for Vice President Al Gore. "We are going to bring about change in U.S. encryption



possible into the coffin. Every time law enforcement case is made more difficult because the perpetrators used unbreakable encryption to cover their tracks, the FBI and police will run to Congress looking for help, warns Washington attorney and former NSA official Stewart A. Baker. "Companies will not have won this fight until they win the fight against 'Mothers Against Stron-

Encryption," he says.

Still, much of the current rhetoric is overblown. For one thing, observes Stephen T. Walker, CEO of Trusted Information Systems in Glenwood, Md., "In spite of all the smoke," export controls on cryptography products—which were once classified as munitions—are already easing. Now, all products that use computer "keys" up to 56 bits long to encode information are freely exportable. That produces a strong enough code for most purposes. And products that have keys of unlimited length (and thus, strength) can be exported as long as they also contain a mechanism for recovering the keys. The situation "is not

FREEH: Without controls, the FBI chief says, law enforcement would be hamstrung

THE ENCRYPTION WARS

FBI AND LAW ENFORCEMENT WOULD:

- Require all encryption products, even those used only within the U.S., to provide "keys" so law enforcers can decode encrypted information and conversations

INDUSTRY AND PRIVACY GROUPS WANT:

- No domestic controls and removal of all existing export controls

POSSIBLE COMPROMISE WOULD:

- Ban domestic controls and relax export controls when similar products are already available overseas

policy," vows Quinn. The group, Americans for Computer Privacy, plans a rollout on Mar. 4.

Is all this firepower necessary? Many veterans of the decade-long encryption battle believe Freeh's plan is too extreme to even take seriously. "Proposals like this are a tremendous stalking horse, but are dead on arrival," says Kawika Daguio, encryption-policy expert at the American Bankers Assn.

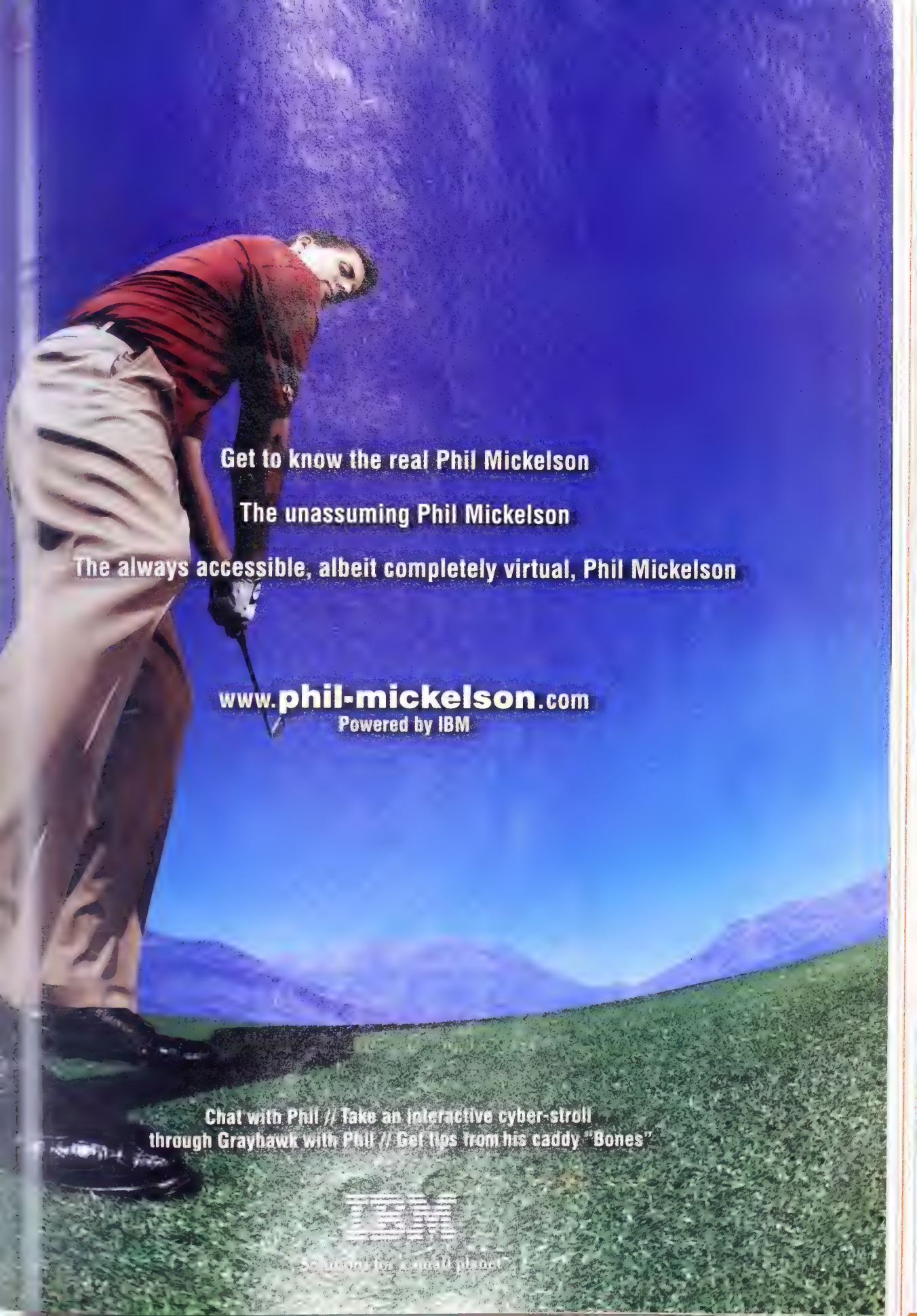
Other players argue, however, that it wouldn't hurt to drive as many nails as

as bad as the zealots on either side would say," says Walker.

Also, a compromise may be in hand. Senators John McCain (Ariz.) and J. Robert Kerrey (Neb.) are currently working on a bill, sources say, that would release exports from controls while similar encryption products are already available overseas. They could also add a ban on domestic controls. "It appears McCain and Kerrey are searching for some way out of what appears to be legislative gridlock," says Commerce Under Secretary William A. Reinsch, who oversees the Administration's policy.

But Reinsch and others are not optimistic that the Senate effort can break the logjam—especially given the neo-cons coalition's hard line. "Aside from Kerrey and McCain, no one wants to compromise," Reinsch laments. "It's the odd thing I've ever seen. Both sides that they are getting stronger—and want to go for the whole loaf." As a result, America's encryption policy will probably continue to be half-baked.

By John Carey in Washington



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DEALMAKERS

CRAZY LIKE A FOX?

Others see trouble at Oxford.
Texas Pacific sees promise

With its ballooning losses and snarled information systems, managed-care pioneer Oxford Health Plans Inc. hardly looks like an investor's dream. But that's just the way Texas Pacific Group likes it.

The \$2.5 billion private investment partnership, led by Fort Worth financier David Bonderman, has a reputation for finding treasures where others see trouble. It has invested in everything from Continental Airlines to Del Monte Foods and Ducati motorcycles.

Bonderman, 55, a former adviser to billionaire Robert M. Bass, declined to comment, but a spokesman says TPG was attracted by Oxford's "preeminent franchise" and growing customer base. TPG planned to team up with Kohlberg Kravis Roberts & Co. But after KKR pulled out, TPG agreed to invest \$350 million for a stake that could reach 22%.

Oxford will be a formidable challenge

for TPG and Norman C. Payson, the new chief that the group will install at Oxford. If history is any guide, TPG will give Payson, former head of Healthsource Inc., lots of running room—but plenty of oversight.

That was the drill at Continental, which Bonderman and his Air Partners investment group led out of bankruptcy in 1993 before forming TPG. Counting a pending deal to sell Air Partners' 14% equity stake to Northwest Airlines Inc., the group has reaped a \$700 million gain on its \$66 million investment in Continental. No wonder TPG is willing to try some surgery on Oxford.

By Wendy Zellner in Dallas

COMMENTARY

By Susan Jackson

NOT EVERYTHING OXFORD DID NEEDS REPAIR

On Feb. 24, Oxford Health Plans Inc. unveiled its bid for salvation. The health insurer that plunged from grace last year found a rescuer in Texas Pacific Group, a Fort Worth investment house that agreed to pump in \$350 million in new capital, and a new CEO in Norman C. Payson, a doctor who once headed Healthsource Inc.

The prognosis remains murky. It's not clear that the bailout, including another \$350 million that Oxford plans to hunt down in the debt markets, will pay all the bills. Oxford lost \$291 million last year on \$4.2 billion in revenues and still owes physicians hundreds of millions of dollars in unpaid fees. Cash flow will suffer at least through 1998 because Oxford is locked into premium prices too low to cover anticipated medical costs. Oxford has "a black hole" in terms of future earnings, says Paul S. Goulekas, a senior vice-president at insurance consultants Conning & Co. **LOSS OF CONTROL.** This is the legacy of founder Stephen F. Wiggins, who resigned as chairman as part of the TPG deal. "I'm an entrepreneur first, a professional manager second," Wiggins told BUSINESS WEEK last August. (Oxford declined to make him available after his resignation.) Indeed, Oxford insiders and analysts blame Wiggins for misjudging the complexi-



FOUNDER: Wiggins was a visionary—but no manager

ty and expense of a crippling computer-systems changeover and, more important, for losing control over the costs of medical claims.

But Wiggins also leaves important assets. He is responsible for innovations that have changed managed care for the better. These are moves that set the Oxford brand apart from rivals and can—if retained—leave a foundation to rebuild upon.

What made Oxford different? Wiggins recognized early on that patients hated the limits of traditional HMO networks. So he bet the company on a more expensive product that

let members seek care outside a core network of physicians. It wasn't a new concept, but Wiggins was the first to make it a key part of his business. The payoff: Oxford's enrollment grew eightfold from 1993 through 1997.

OPEN EAR. Wiggins also understood that customers would pay more for decent service—an aspect of the business that insurers were infamous for ignoring. Modeling Oxford's marketing after consumer giants such as American Express Co., Oxford studied what its members wanted, and listened. One masterstroke: an alternative-medicine initiative that led members to discounts on such services as acupuncture. It cost Oxford almost nothing,

but gained widespread attention.

Oxford still must clean up Wiggins' very ugly operational mess. "We've got some work ahead of us," Payson admits. Yet Oxford remains a vibrant presence in the market. For all the bad news, membership grew 8% between last Sept. 30 and Jan. 1, to 2.1 million. Give Wiggins some credit: If Oxford can survive the financial pitfalls of the next year, the legacy of his market savvy promises to help it make a full recovery.

Jackson is BUSINESS WEEK's Connecticut correspondent.



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MARKETING

THOSE NEW BREWS HAVE THE BLUES

A shakeout is coming in the saturated designer-beer market



By some estimates, there are 300 microbrews named after animals or fish. Dozens more are flavored with everything from strawberries to pumpkins. "I can't choose," laments Chicago carpenter, disk jockey, and beer lover Rick Lidinsky, who switched from micros to imports. "The market is saturated."

That confusion spells trouble for all those companies created to quench one of the hottest trends of the '90s: consumer thirst for fuller-bodied, not-just-another-Bud brews. After meteoric growth of about 50% a year in 1994 and 1995, the microbrew industry has gone about as flat as day-old beer. Sales edged up just 5% last year, according to newsletter *Beer Marketer's Insights*. The stocks of the dozen or so specialty brewers who poured into the market in recent years have lost their heads.

In recent weeks, such industry leaders as Pete's, Pyramid, and Redhook—all on the West Coast—have reported declining beer sales and restructuring-related losses for 1997. Even the healthiest of the microbrewers, Boston Beer Co., brewer of Samuel Adams, saw its sales and earnings fall and is focusing its marketing dollars on a narrower line.

Now, a full-fledged shakeout is on tap

among brewers and brewpubs—whose numbers have jumped fourfold, to 1,306, since 1993, according to the Institute for Brewing Studies. In late January, a small Maryland brewer, Frederick Brewing Co., bought out two even smaller rivals to form a mid-Atlantic regional. More significantly, on Feb. 19, No. 2 Pete's, brewer of Pete's Wicked Ales, hired Morgan Stanley, Dean Witter, Discover & Co. to explore its options, including mergers. "We need to get larger to gain more focus from distributors and retailers," says Pete's President Scott Barnum. He figures the top 12 micros will be whittled down to six in short order. Adds John Hickenlooper, CEO of Denver's Wynkoop Brewing Co., a microbrewer and brewpub operator: "It's a jungle. Only the strong will survive."

A GLUT? What went wrong? Tantalized by consumer fancy for every imaginable new concoction, and with easy access to capital, micros churned out as many as 4,000 different brands. Entrepreneurs were hard pressed to

handle growth and quality problems began to creep in. Many drinkers returned to imports. "We were a mile wide and an inch deep," says Barnum of Pete's. The brewer has recently dropped 4 of its 12 brands.

The micros also got squeezed hard by distributors and retailers, who are pruning product lines to focus on the most lucrative brews. Zimmerman's, big Chicago beer and liquor distributor, has dumped all but six of the 75 micros it carried three years ago. "Unless it's heckuva brand, I don't want another [micro]brew in my house," says Kevin Burke, owner of Miller Brewing Co. distributors in Chicago, San Francisco, and Louisville.

Attempting to catch the fad's coattails, Anheuser-Busch, Miller, and Coors have launched or taken stakes in their own microbrews. Their forays have not been very successful, but they continue

GOING SKUNKY
Even micro leaders such as Redhook have reported declining beer sales and losses for 1997

to roil the market because of their close relationships with distributors. In Anheuser's case, the company netted a lawsuit. Four California micros are suing Anheuser-Busch Co. for restraint of trade because the beer giant was offering

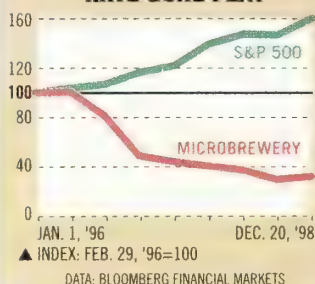
financial incentives to distributors who signed on as "exclusive" sellers of Anheuser brands and authorized micros. The Justice Dept. is also investigating. Anheuser-Busch denies the charge (BW—Feb. 23).

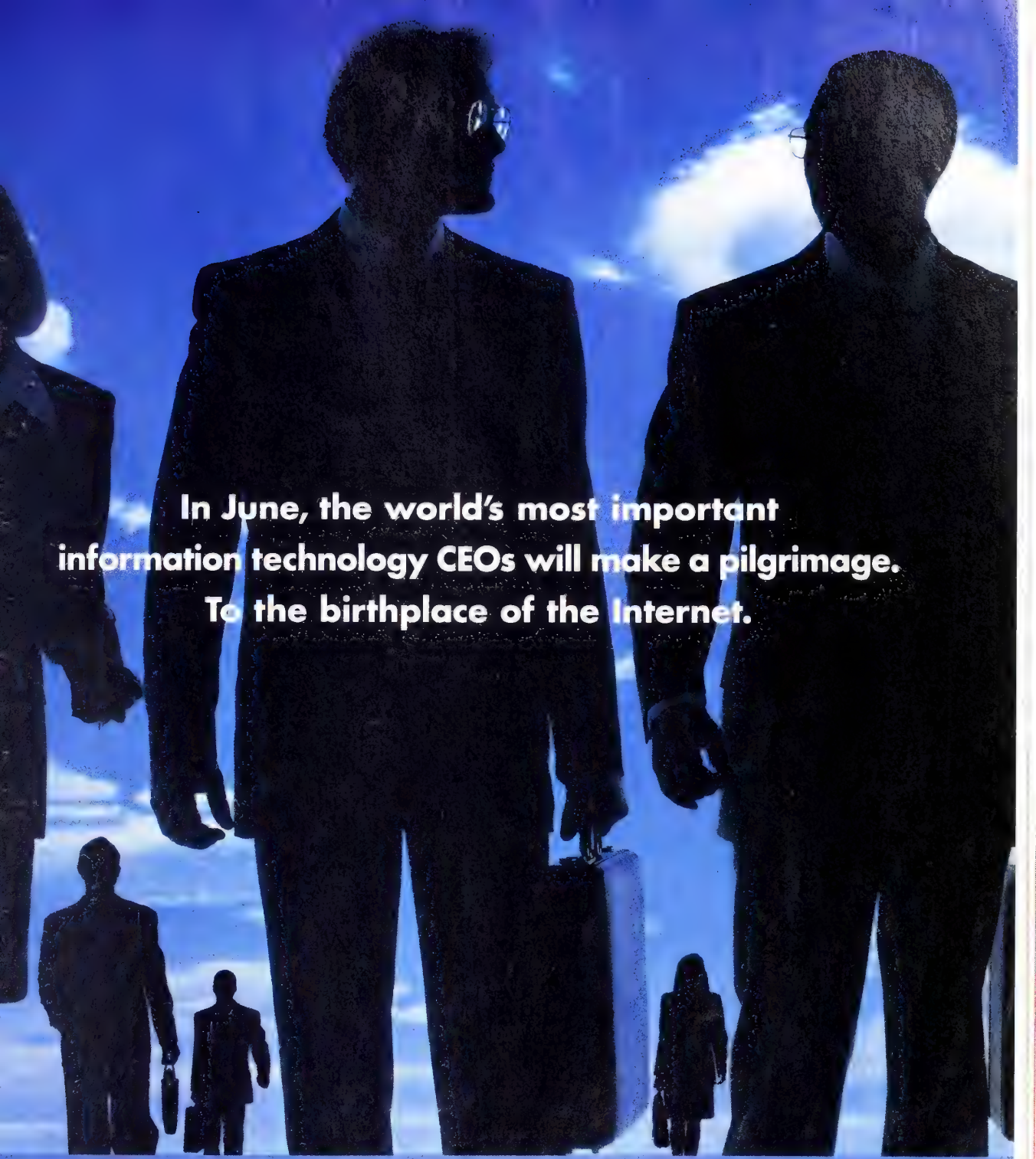
Who will survive the pub brawl? Many industry execs speculate that among the survivors will be Boston, the only micro with a truly national franchise, and longtime California micros Sierra Nevada and Anchor Steam. Some expect that Pete's and Pyramid may merge. Miller is also shopping for a stake in a West Coast micro. Paul S. Shipman, Redhook Ale Brewery Inc. founder and chairman, may have crafted a key survival strategy seven

years ago by selling 25% of his company to Anheuser-Busch and gaining a distribution network. But even Redhook is saddled with more than 50% excess capacity. At least we all now know the answer to the pressing philosophical debate: Can there be too many beers?

By Richard Melcher in Chicago

MICROBREWERY STOCKS HAVE GONE FLAT





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CARMAKERS

IN REVERSE AT NISSAN

It has fallen way behind Japanese rivals in the U.S.

For a while there, it looked as if Nissan Motor Corp. USA had gotten its act together. After the dog days of the early '90s, it launched its first successful family sedan, the Altima. The bread-and-butter Nissan brand pulled ahead of the archrival Honda line in 1993, and its Infiniti luxury cars continued to rack up impressive annual gains. Then, 18 months ago, it launched \$200 million worth of edgy image advertising designed to put the Nissan name more firmly on the map. The prize-winning series featured the happily enigmatic "Mr. K" and his sidekick Jack Russell terrier.

That picture of progress began to unravel in 1996, when Nissan's market share dipped from 5.2% to 5%. And in 1997, Nissan shifted into reverse. Despite a healthy North American car market and the advantage that imports gained from the rising dollar, Nissan sales slipped nearly 3%, to 728,377 ve-



MR. K AND POOCH: Hot ads didn't translate into sales

hicles. Meanwhile, Toyota Motor Corp. sales rose 6% and American Honda Motor Co.'s, 11%. Both companies posted North American sales records. Now, says George Peterson, president of market researcher AutoPacific Inc., Nissan isn't "really a first-tier Japanese competitor anymore."

REVOLVING DOOR. Nissan has two big problems: un compelling products and unstable management. The latest change came on Feb. 20, when Minoru Nakamura, president of U.S. holding company Nissan North America Inc., announced the early retirement of three key execs—including the general man-

ager of the Nissan Div., which does an estimated \$15 billion in sales a year. That division's new chief, who will take over on Mar. 2, will be the third in less than three years. The revolving door at Infiniti—where sales rose 17%—is rotating even faster, with five managers over the past four years.

Much of the blame, however, can be traced back to Japan. While the Toyota

Camry and the Honda Accord have gotten roomier to take on the Ford Taurus, Nissan's Altima has become the runt of its class.

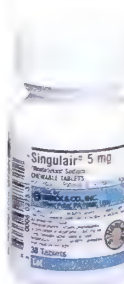
Things are not likely to change any time soon. Nissan will bring three new models to market this year, but in categories where Japanese carmakers tend to have low volumes: a minivan, a low-end luxury sedan, and a V-6 pickup. In the ad for the new truck, the pickup rolls over Mr. K, who is emerging from a manhole. "Dogs love trucks," he says. Unfortunately for Nissan, they can't buy them.

By Larry Armstrong in Los Angeles

PHARMACEUTICALS

MERCK HOLDS ITS BREATH

A new asthma pill has the potential to be a blockbuster



Wall Street was panting. On Feb. 23, Merck & Co. stock soared nearly 5%, to 130%, after the Food & Drug Administration gave the company marketing approval for a new asthma drug, Singulair. Cowen & Co. analyst Stephen M. Scala figures it could generate worldwide sales

of \$1.5 billion by 2001.

Why the hoopla? The incidence of asthma in the U.S. is soaring. According to the National Center for Health Statistics, the number of asthma sufferers rose from 10.4 million in 1990 to 14.6 million in 1994. And Merck's drug is the first of the new leukotriene-blocker drugs

to be approved for children 6 and up—a large and growing market.

The most common treatment for asthma is inhaled steroids. But long-term high doses may cause such side effects as glaucoma, osteoporosis—and, for kids, impaired growth. Singulair and similar compounds work by blocking leukotrienes, molecules involved in the inflammation associated with asthma.

"This whole class of drugs is a big step forward," says Dr. Jeffrey M. Drazen, a professor at Harvard Medical School.

So far, the only leukotriene blocker on the market, Zeneca Pharmaceuticals' Accolate, has not been a blockbuster. It generated sales of just \$77 million in 1997, according to research firm IMS America Ltd. Dr. Beth Seidenberg, Merck's executive director for clinical research, points out that Accolate—unlike Singulair—was not approved for children under age 12. Accolate is also



O.K. FOR KIDS: A growing market

associated with incidences of liver toxicity when taken at four times the approved dose, a problem that hasn't shown up in Singulair. Seidenberg says the Merck drug will be a great option for children whose parents worry about stunted growth. And Singulair may help adults taking high doses of inhaled steroids to cut back.

Still, can Singulair

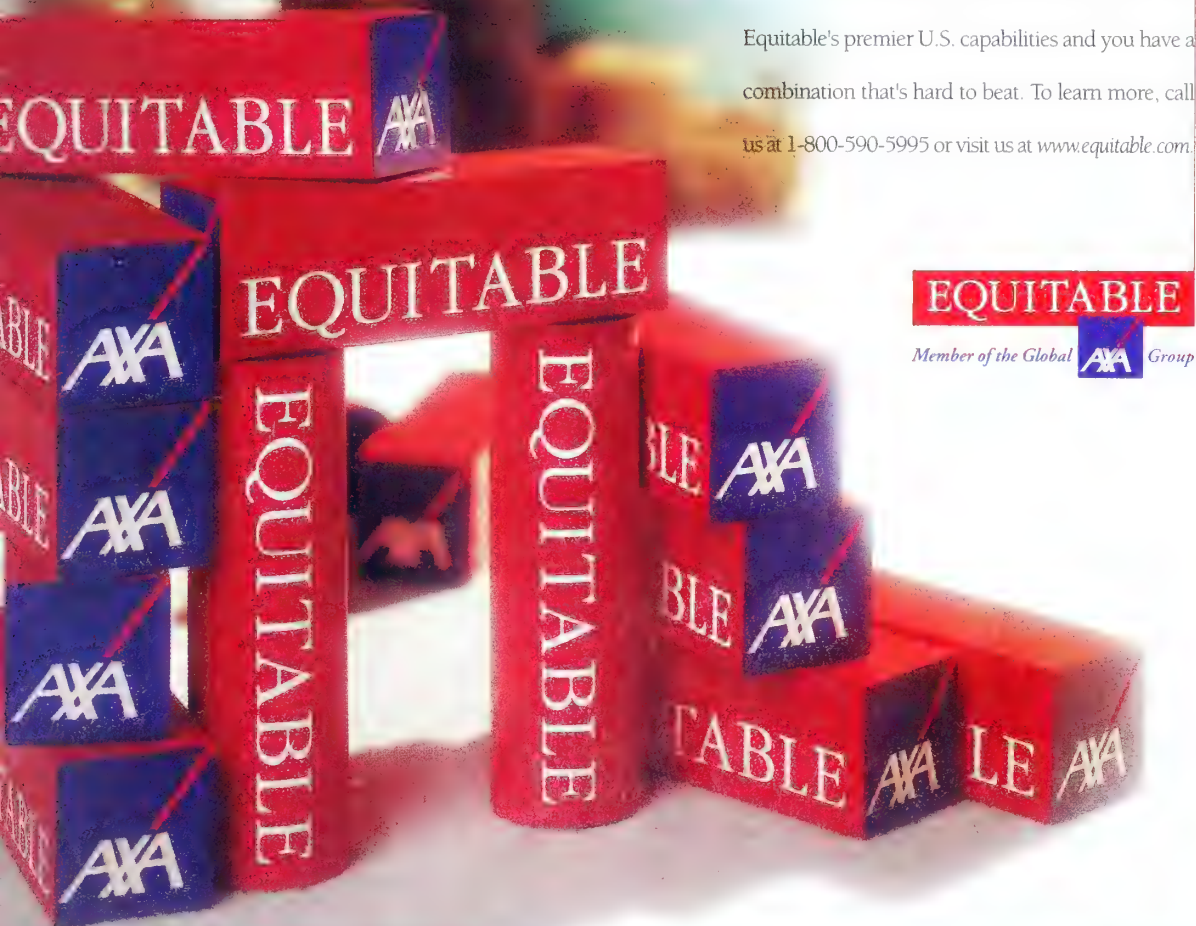
live up to the Street's expectations? Many patients do well on inhaled steroids, so their doctors may see no need to alter treatment. And any possible long-term side effects may not be known for years. "It's promising, but [its] place in long-term asthma treatment is not fully defined," says Dr. David M. Lang, division chief for allergy and immunology at Allegheny University. It has proved capable of putting air in Merck's stock, though.

By Amy Barrett in Philadelphia

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MESSY ACCOUNTS AT WASTE MANAGEMENT

GARBAGE IN, GARBAGE OUT. That's one way to look at Robert "Steve" Miller's harsh assessment of "serious accounting errors and errors of judgment" at Waste Management. On Feb. 24, the interim chairman and CEO of the big hauler, who took the reins on Oct. 29, restated five years of earnings and announced \$2.9 billion in aftertax write-offs. Waste, reeling from brutal competition, had been overstating the value of its assets and understating its environmental liabilities. The company has initiated talks with the Securities & Exchange Commission about the past accounting, though no formal

investigation is under way. With the big cleanup behind him, Miller insists the future is brighter: "There is growth in our core business, though it's not Silicon Valley."

CURTAINS FOR NEW CENTURY

IT WAS SUPPOSED TO BE A model for providing news online and a way for newspapers to protect their turf against the likes of Microsoft. Instead, New Century Network became a money pit and a source of infighting among the nine partners—including *The New York Times*, *The Washington Post*, Gannett, and Knight-Ridder. So on Feb. 25, less than a year after the launch, the site went dark. The idea had been to post the best stories from 140 newspapers on a single site. But the partners wrangled constantly and ultimately lost \$27 million.

CLOSING BELL

JUST NOT DOING IT

Nike is jogging on jagged terrain. In the first three weeks of February, the stock rose from 41½ to 46½, partly on rumors that Warren Buffett was buying. But on Feb. 24, Nike said third-quarter and yearend earnings would be below analysts' estimates—and layoffs and other cuts would ensue. The stock dropped to 43½ in after-hours trading. What was Nike's Achilles' heel? Excess inventory, especially in the U.S. and Asia. Nike had been hoping to double Asian sales but now expects them to be flat.



DRUG DEALS THE FTC MAY NOT SWALLOW

CREATING MORE EFFICIENT health care is a top priority in Washington. But Federal Trade Commission staffers fear that proposed mergers among the top four drug wholesalers might be a bit too efficient—a prescription for higher prices and slower deliveries. Sources close to the case say FTC staff will recommend that the board block Cardinal Health's proposed merger with Bergen Brunswig and McKesson's buy of AmeriSource Health. These companies control 82% of the \$66 billion industry. The FTC's decision could come on March 3.

CREDIT UNIONS GET THEIR WINGS CLIPPED

SCORE ONE FOR THE BANKS IN their battle against credit

HEADLINER: JAN LESCHLY

THIS ONE DIDN'T CLEAR THE NET

Jan Leschly is on the defensive. Following the acrimonious Feb. 23 collapse of merger talks between Smith-Kline Beecham and Glaxo Wellcome, Leschly, a tennis pro turned Smith-Kline CEO, is under pressure from investors to get a deal.

Leschly nixed the Glaxo deal after a Feb. 20 meeting with Glaxo CEO Richard Sykes in which, a former SB insider says, the exec discovered that the proposed combination was "not a merger, but a takeover." But investors were upset that the deal had come apart: They

knocked SmithKline's value down by \$6.6 billion.

SmithKline is profitable—earnings rose 17%, to \$2.7 billion, in 1997—but it ranks ninth in prescription-drug sales, down from third in 1989. And while its investments have

turned up many leads for new drugs, SmithKline lacks the R&D funds to pursue all of them.

Roche Holdings, Schering-Plough, Warner-Lambert, and Britain's Zeneca are all possible partners. Now, Leschly, 57, has to prove he can fight back from two sets down.

By Julia Flynn



unions. On Feb. 25, the Supreme Court upheld a federal law barring the unions from expanding their membership beyond persons who work in the same occupation. In a 5-4 decision, the court noted that the 1934 law that established the credit unions required that their membership be limited to groups "having a common bond of occupation or association." In 1982, credit unions started letting small businesses join. Bankers sued, arguing that any number of people could join credit unions, which offer many bank services but which are tax-exempt.

BEN & JERRY'S ICES A DREYER'S OFFER

ON FEB. 24, BEN COHEN AND Jerry Greenfield, the self-described former hippies who founded Ben & Jerry's Homemade, put the deep freeze on an offer from Dreyer's Grand

Ice Cream, Ben & Jerry's largest distributor. Since the arrival of a new CEO a year ago, Ben & Jerry's, the maker of such funky super premium flavors as Chubby Hubby and Wavy Gravy, has halted a financial meltdown that has resulted in five straight quarters of declining profits. But spurning Dreyer's may launch Ben & Jerry's down another rocky road, putting pressure on the relationship between the two companies.

ET CETERA...

- To ARMS: Intel is licensing a low-priced microprocessor design, the ARM chip.
- General Motors' Delphi Automotive Systems will sell its seating business to Lear.
- Allstate is seeking \$10 million in damages from alleged insurance scamster.
- Toys 'R' says fourth quarter earnings will be hurt by high promotional spending.

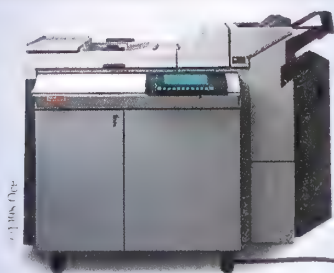
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ED BY OWEN ULLMANN

PATIENT'S BILL OF RIGHTS: BUSINESS GETS OUT THE SCALPEL

When Corporate America launched a massive lobbying blitz to block sweeping regulation of managed-care plans in late January, it looked like a loser. HMOs, other employer health plans were on the run as consumers, doctors, and pols cast them as the villains in a world of bare-bones medicine. The public mood was down at the cineplex as audiences cheered Helen's character in *As Good As It Gets* when she blasted an doctor for limiting her child's treatment. In a few short weeks, corporate forces staged a remarkable comeback. Through political jockeying, business has stalled the rush to impose new rules on health care. While Congress is still likely to enact a patient's bill of rights this year, the final package will be much more to employers' liking.

That's no mean feat. President Clinton's version of the patient's bill of rights gets plenty of use for its call for easier access to specialists and treatments. And a physician-friendly, bipartisan alternative that's even tougher than HMOs has 216 House sponsors.

UNWIDATED. To stem the tide, business lobbyists argue that the GOP bill, the Patient Access to Responsible Care Act (PARCA), would undermine the managed-care networks that have halted the double-digit medical inflation of the 1980s. PARCA's backers—a coalition of medical and consumer groups—maintain that the measure would cost no more than 2.6%. But actuaries Milliman & Robertson Inc. conclude that the bill would hike premiums by 4.6%. A boost that large would induce 46% of small companies to drop health insurance, according to a poll released on Feb. 24 by the business-backed Health Benefits Coalition.

Those figures may be self-serving, but companies are using them to chip away at PARCA's support. They've teamed up with Senate GOP Whip Don Nickles (R-Okla.) and House Ma-

jority Leader Dick Armey (R-Tex.), who were furious that Senator Alfonse M. D'Amato (R-N.Y.) and 90 Republican House members—all up for reelection this fall—backed the measure. Now, two GOP co-sponsors have dropped out, and "many, many others have told us privately that they wish they hadn't signed on," says small-business lobbyist Dan Danner. Business, laments a Senate Democratic staffer, "has intimidated" Republicans sympathetic to HMO reform.

Corporate America still faces a formidable foe: Bill Clinton.

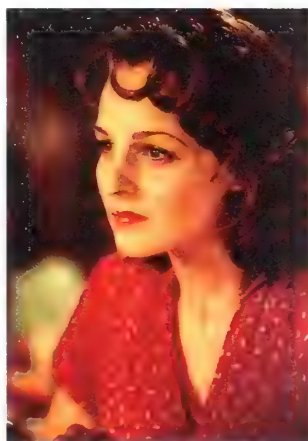
His bill of rights would require health plans to give members detailed information about physicians, hospitals, and claims processing. It would mandate external appeal boards when health plans deny coverage. The package also would make it easier for patients to see specialists and to win payment for emergency-room visits even when they're false alarms. On Feb. 20, Clinton ordered that his rules apply to health plans covering 87 million federal employees, veterans, and Medicare and Medicaid recipients.

But business won't willingly follow suit. It sees the bill of rights as part of a Clinton plan to win what he couldn't get in 1994—sweeping health-care reform—one step at a time. The Business Roundtable wants a purchasers' coalition of large employers—excluding insurance, HMOs, and drug companies—to draft patient-protection rules that companies would

pledge to meet voluntarily.

That won't satisfy politicians eager to ride the tide of HMO resentment. The Dems plan to make patient rights a centerpiece of their fall campaigns. And a GOP strategist concedes that such legislation "is a political imperative." With both parties aboard, some version seems bound to pass. Business may have defused the anti-HMO explosion—but it won't escape unscathed.

By Mike McNamee, with Richard S. Dunham



HUNT: *The people's voice*

CAPITAL WRAPUP

THE PAXON SHOCKER

Even months after surviving a coup attempt, Speaker Newt Gingrich is rapidly consolidating his once-rocky hold on the House. Latest good news for Newt: the surprise retirement of Representative Bill Paxon (N.Y.) on Feb. 25.

His departure will remove the No. 1 threat to Gingrich's leadership. Paxon has been working to topple Newt's top lieutenant, House Majority Leader Dick Armey (R-Tex.). Paxon, who lost leadership post after meeting with

the coup plotters, says he wants to spend more time with wife, Susan Molinari, and family. Molinari left the House last year to become a news anchor. "The priority of family must now take precedence," said Paxon. "I will never run for office again, never, not even for dog warden." Another reason: Armey—with Newt's help—is likely to keep his post after the elections.

Gingrich can now focus on plotting '98 House races and his 2000 Presidential bid. "With Paxon off the horizon, there's no immediate threat," notes congressional analyst Charles Cook.

Except from his own image: Gingrich remains hugely unpopular, though focusing on issues such as better schools has helped. And, says Republican pollster Whit Ayres, "He has been very smart to keep his mouth shut on the Clinton scandals."

Inside the House GOP, Newt is stronger than at anytime since the 1995-96 government shutdowns, though conservative dissidents vow to keep up pressure. Says one GOP strategist: "Newt doesn't have to watch his back at every turn—just at every other turn." By Richard S. Dunham

CAR TROUBLE

The boom is a bust. And scared consumers have stopped buying

The perfect market. That's how the world's carmakers viewed Asia until just a few months ago. Rising incomes, hundreds of millions of potential buyers—the ingredients seemed in place for the biggest car-buying binge in automotive history. The Japanese, Europeans, Americans, and Koreans all rushed to get in on the bonanza before it was too late.

Now, the boom has turned into a bust because of a currency crisis that has devastated many local economies and prompted scared consumers to shun big-ticket items like cars. In Japan, dealers are desperately seeking customers, while the Chinese are selling their most popular car, the locally made Volkswagen Santana, for 25% less than two years ago. Sales are evaporating in Thailand, Malaysia, and Indonesia. Giants like Toyota Motor Corp. and Ford Motor are grimly enduring the recession, while the national car companies of Indonesia and Malaysia face their roughest road test yet.

It's time to rethink strategies. Both Ford and General Motors Corp. want to win a 10% share of Asia's market in the next decade or so. Local production is a must, so why not pick up someone else's capacity cheap, especially in hard-

hit Korea? Thus Ford is talking to Samsung and Kia, while GM is dancing with Daewoo Motor just six years after a bitter corporate divorce. Says Alan Periton, president of GM Korea: "Trying to go it alone just doesn't make sense."

Meanwhile, the Japanese have spent billions creating an Asian auto industry from scratch. Nine out of 10 cars and pickup trucks in the region are made by Japanese companies, and they want to keep it that way. "We are not going to flee," says Honda Motor President Nobuhiko Kawamoto.

So Japan's carmakers are flying hundreds of Thai workers back to Japan for additional technical training and extending support to local suppliers to revamp their operations for export. Even before Ford and GM get rolling in Thailand, "the Japanese are digging in even deeper," says Michael Dunne, president of Automotive Resources Asia. **THAI CONCEPT.** Yet the Japanese also have problems. They want to source all their parts locally: That way, a Thai plant won't have to spend huge amounts of depreciated baht to buy parts from Japan. Far better to buy locally and earn hard-currency profits in Japan, the U.S., or Europe. It's a good idea, but it needs work. Japan's carmakers in Thailand get only 70% of their parts locally, and their locations in Indonesia and the Philippines have much lower local content and so practically no cost advantage.

The cost of staying in Asia's auto markets will keep climbing as sales contract further. Carmakers have a choice: stay in the race or end up as roadkill.

By Emily Thornton in Tokyo

THE SLUMP IN CAR SALES

CHANGE IN UNITS SOLD 1997-1998*

THAILAND

-51%

MALAYSIA

-51%

INDONESIA

-49%

PHILIPPINES

-21%

SOUTH KOREA

-16%

*DATA FROM AUTOMOTIVE NEWS & ANALYSIS
MOTOR VEHICLE NEWS & ANALYSIS
ING BARINGS HOKAI MOTORS



THE BIG CRUNCH IN THAILAND

You get a sense of how bad Thailand's recession is soon after entering Mitsubishi Motors Corp.'s regional offices in suburban Bangkok. To save on electricity, the hallways are unlit and air conditioners are set a few degrees warmer than usual. The fourth floor, once home to spacious office suites with special executive showers and washrooms, is closed completely. An ominous sign asks, "How can we survive?" The company is shutting assembly lines and laying off hundreds of workers.

The worst is yet to come. After a dismal 1997, Thailand's automobile market is still shrinking. Demand could drop to 160,000 units this year, one-third the number sold in the peak year of 1996. That's even less than the capacity of Mitsubishi's four Thai facilities, not to mention the 10 plants of its Japanese and American rivals. And with demand plunging everywhere else in Southeast Asia as well, export prospects are bleak. "How can we survive?" asks Susumu Nakagawa, Mitsubishi Thailand's executive vice-president.



THAILAND'S CAR CRISIS

VANISHING SALES

Sales may not even reach 160,000 vehicles this year, a third of 1996 results. A big rebound will not occur until 2000.

OVERCAPACITY

Japanese and American companies will soon be able to make 1.2 million vehicles a year in Thailand.

WEAK EXPORTS

They will eventually pick up, but for now, even the Japanese are too pinched to buy many Thai-made cars.

DATA: BUSINESS WEEK

not everybody will. After the world's car makers poured billions into Thailand to grab a share of the domestic market and produce for the entire region, the country now has a capacity that will last well into the next century. Major new factories by late-arriving General Motors Corp. and Ford Motor Co. are still going up in the pineapple fields of an industrial estate two hours southeast of Bangkok. It will soon help push Thailand's total capacity to 1.2 million cars and trucks, says Dennis Meseroll, associate director of Brooker Group, a Bangkok consulting company.

IN, NOT OUT. It looks grim. But so far, no auto makers have decided to cut production. Instead, they are scaling back production. GM, for example, slashed planned output of Opel passenger cars from 100,000 annually by 20% to 40,000 and reduced its investment by one-third, to \$500 million, in building a smaller plant and deepening production. Meanwhile, to keep operations from deteriorating further, Japanese carmakers are dropping shifts, bailing out wobbly parts makers, and setting up consumer credit to prop up dealers and push sales. Yet reducing output won't solve problems, since car plants require large production volumes to pay off. "Because

the auto industry is capital intensive, you want to be running full bore to make money," says Brooker's Meseroll. Right now, the industry is running at just 30% capacity. "People are in big trouble," adds Meseroll.

The government has not made the auto makers' task any easier. Because of the fiscal policies mandated by the International Monetary Fund, the Thais have increased value-added taxes, excise taxes, and import duties on goods, including cars. Some carmakers, such as Toyota Motor Corp. with its Corolla, are swallowing these costs and actually lowering prices. Others, such as Chrysler Corp. with its Jeep Cherokee, are passing on the costs, adding as much as \$20,000 to the retail price. Neither approach helps profits.

Even before the crisis, the signs of a weakening market were appearing. Honda Motor Co.'s experience with the City, a four-door car unveiled in 1996, is a case in point. The simply designed, \$8,300 City is made specifically for Southeast Asian buyers in a \$100 million plant near Ayutthaya. "We were hoping to create a new passenger-car market," says Satoshi Toshida, president and CEO of Asian Honda Motor Co. Yet in the past two years, only 30,000 were sold—

GOING, GOING...

Repossessed cars are auctioned off in Bangkok. Credit has become difficult to find

way below expectations.

Carmakers still haven't given up hope that exports will help compensate for weak local sales. The question remains: Export where? Unlike Mexico, which survived the 1994 peso crash thanks in large

part to the North American Free Trade Agreement, Thailand does not have a huge open market right next door. True, Japanese auto makers can use their Thai factories to supplant more expensive assembly lines at home. Toyota Motor Corp. wants to sell 22,000 Thai-produced pickups in Australia and New Zealand, replacing trucks that came from Japan. Yoshiaki Muramatsu, president of Toyota Motor Thailand Co., thinks that he might be able to export to smallish markets like Sri Lanka or the Middle East.

TIGHT MARKETS. But the quantities being talked about are small, and demand is slow in Japan as well. Longer term, carmakers are looking forward to 2003, when tariffs on cars traded within the Association of South East Asian Nations are supposed to drop to 5% and Thailand can export freely to nearby markets. But even if trade barriers are dismantled as promised, any relief is still years away.

Cracking developed countries will be difficult, too. Despite the cheap baht,

Thai factories are too small to compete efficiently with the giant auto facilities in the U.S., Japan, or Europe. Concedes one top car executive: "We are all going to meet each other on a street corner in a foreign country and find that we are all trying to do the same thing." Says David L. Snyder, president of Ford Operations (Thailand) Co.: "We don't want to become a company that's just exporting out of Thailand."

When the Thai market finally does recover, those carmakers still standing should profit from a surge in pent-up demand for new vehicles. "That hope is still there," says Mitsubishi's Nakagawa. "But at this moment, it is rather difficult to expect that." Instead, Nakagawa can only soldier on, waiting for a comeback and looking forward to the day he can turn on a few more lights.

By Bruce Einhorn in Bangkok

A WRONG TURN IN MALAYSIA

It was, perhaps, the high point in the history of Perusahaan Otomobil Nasional, or Proton, Malaysia's national carmaker. At a secret ceremony last November outside Kuala Lumpur, the first \$200,000 Lotus Elise sports coupe rolled off a Proton assembly line. The Malaysians, who bought control of the British auto maker in 1996, had worked with Lotus engineers to build an assembly line for the sports cars in Malaysia. The move was supposed to showcase Proton's ability to make one of the world's most sophisticated cars, open up a new luxury segment and follow a fiscal year when earnings more than doubled on sales of \$1.6 billion.

The currency crisis has changed all that. In the latest statistics, Proton's January car sales dropped 13%. Annual profits could drop as much as 20% in the fiscal year ending in March, and another 60% next year, as Malaysian car buyers feel the sharp pinch of recession. Despite delays, the company still plans to increase capacity from 230,000 to as much as 1 million cars a year, and make everything from cheap minicars to Lotus exotics. But it's hard to see who will buy those cars in this recession, which could last years. Proton executives still have high ambitions. The question is how much ambition this company can afford.

PRINCE CHARMING? Proton still has \$261 million in cash on hand and has relatively modern plants that can spit out Mitsubishi-designed cars. It may pick up some extra sales as affluent Malaysians trade down to cheaper vehicles. Last November, Saudi Prince Alwaleed bin Talal bin Abdulaziz Al Saud

bought a 3% stake. The Prince, says one Proton manager, will "put our name up in lights alongside Michael Jackson, Euro Disney, Canary Wharf," and his other moneymakers.

But to be a front-runner, a company needs a strong market, efficient manufacturing, and the latest technology. Proton is struggling on all three fronts. Total demand in the Malaysian car market may drop 40% to 50% this year. Melding together an engineering

locally made parts than to import them, because of inefficient local suppliers. Now, with the depreciation, the cost of imported parts will go up as well.

Until the crisis, none of this mattered. Because of tariffs on imported cars, Proton—which is part of the conglomerate DRB-Hicom Group—had a great business. After Chairman Yahaya Ahmed's death in a helicopter crash in 1997, an old associate, Mohamed Saleh Sulong, immediately took over. But don't look for big changes anytime soon. Saleh makes it clear he is keeping the chair warm for Yahaya's young daughter Yatina, who now has a seat on the board of DRB-Hicom: "We're giving her the opportunity to take the leading role."

Yahaya's daughter will have a lot on her hands. As the crisis deepens, every auto maker is trying to export its way out of a sales slump. Yet overseas, Proton must compete with better-known low-enders such as Hyundai—whose prices will also fall because of the weaker Korea won. "I applaud Proton's ambition. They've tried like mad to get somewhere. I just wonder if they're not up against a tiger or something bigger,"

says John Bonnel, analyst at Automotive Resources Asia in Bangkok.

Some say Proton has to focus on what it

STUCK IN PARK?

As temporary chief, Proton's Saleh won't be making any big changes

team from Britain's Lotus, Japan's Mitsubishi Motor., and France's Citroën has also been a challenge. Eventually, Proton intends to blend the three countries' technologies into a single car that is still in the design stage. However, the engineers avoid eye contact with their foreign counterparts at the vending machines. Yoshifumi Kawashima, the Mitsubishi executive in charge of the southeast Asian division, says he has no problem with Proton's new Lotus division. Yet one Proton executive says privately, "Anyone can see Mitsubishi is not happy we bought Lotus."

Coupled with the management problems are serious bottom-line issues. It has long cost Proton more to acquire

does best: assemble Japanese-made cars for the low end of the domestic market. Yet this does not seem likely. Proton has delayed by up to 36 months it plans to build the huge new Tanjung Malim facility. But it is not canceling them. Proton still wants to be world class. In an age of survival, such visionary thinking could be dangerous.

By Michael Shari in Kuala Lumpur with Heidi Dawley in London



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GO WEST, YOUNG FRENCHMAN

When Eric Di Benedetto got his degree from the Essec Graduate School of Management in Paris, he was one of a handful who headed straight for Silicon Valley. That was 1989, and Di Benedetto knew that in France, 15 years might pass before he could assume any serious responsibilities. In California's high-tech mecca, by contrast, his career took off. Last year, the 32-year-old expat launched his own venture firm, Convergence Partners, with two U.S. colleagues—and had a \$60 million fund the day it was born.

From Paris to Aix-en-Provence, the word is out: Silicon Valley holds all the promise the French economy lacks. And what began as a trickle of entrepreneurs and high-tech talent is becoming a torrent. For the new expats, the trip westward brings not only well-paid jobs but the chance to ride a high-tech revolution into the next century. For France, though, the trend is ominous. "The whole environment in France is tragic," says Alex Balkanski, a French transplant whose C-Cube Microsystems Inc., founded in Silicon Valley a decade ago, is now a \$340 million company. The tech gap between the U.S. and France, he says, "is not closing, it's getting wider."

elite graduates are leaving, placement executives say. And a recent poll shows 77% of French youth would take a job overseas if it meant a promotion. Small wonder: Di Benedetto says a typical French business grad earns half the salary of a new MBA in the U.S.

STARTUP HEAVEN. A brain drain of this magnitude is a serious blow for France. It is already struggling with 24% unemployment among those under 26, a business culture hostile to entrepreneurs, and an underdeveloped high-tech sector. Yet these are the very problems driving engineers, programmers, and MBAs to vote with their feet. In effect, France is hemorrhaging its lifeblood—the people it needs to create new jobs and industries.

Many exiles head to Silicon Valley, where some transplants are noted executives: 3Com chief Eric Benhamou, for instance, and Borland founder

In effect, France is losing its lifeblood—the people it needs to create jobs

Philippe Kahn. The number of citizens registered with France's consulate in San Francisco quadrupled, to 40,000 between 1991 and 1996. Many more may be unregistered, French techies say.

Some of the high-tech startups that have sprouted in France are also shifting offices and operations to Silicon Valley or cities such as Boston. Aplio Inc. was founded in France 15 months ago but is building up its activities in the U.S. from a San Bruno (Calif.) headquarters. "I can build a company in one to two days in the U.S.," says CEO Olivier Zitoun, a 30-year old expatriate

Last year, after Zitoun helped launch a device allowing telephones to send calls via the Internet, Aplio was featured in a spot on national television. It was just the kind of fame Zitoun needed to be reminded that he wasn't in France, where small companies are viewed as unreliable. "Most people here didn't even know we were a startup—French," says Zitoun.

To be sure, the French exodus in part reflects a desire among young managers to gain international experience—a desire that may eventually take it home. On that assumption, government officials applaud the trend. Instead of worrying, competent ministers say the diaspora will create a savvy generation of French executives. But educators, economists, and entrepreneurs warn that of those fleeing, many won't return to France.

Count venture capitalist Di Bened-
to among them. "The French model
not working," he says flatly. Such a
buke is easily dismissed in Paris. The
French government would do better
find ways to keep its bright people
home if it wants a dynamic economy.

By Gail Edmondson in Paris



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EDITED BY JOHN TEMPLEMAN

HAT A DEAL WITH IRAQ WON'T FIX: THE WEAPONS BUILDUP IN IRAN

the deal that U.N. Secretary General Kofi Annan cut with Iraqi strongman Saddam Hussein on Feb. 22 won't end the weapons buildup in the Middle East. Saddam's continued efforts to develop chemical and biological weapons are a greater threat to his neighbors than to the U.S. or Europe. So they're arming themselves. Egypt, Israel, and Saudi Arabia all have medium-range missile systems.

Iran's weapons program, however, is the boldest. So bold, in fact, that it alarms both Iran's neighbors and the U.S. Washington believes Iran is receiving knowhow from Russia. That's why the Administration because Russia has been working to increase its Middle East clout at a huge expense by moves such as its in-entrenchment in the Iraq crisis.

Consequently, Iran's program will remain high on the agenda when Russian Foreign Minister Viktor S. Chirkin visits Vice-President Al Gore in Washington on Mar. 10. And on by Israel, Washington is pressing on Moscow to stop Tehran's missile program. The pressure is mounting because Iran's Shahab-3, developed from North Korea's No Dong missile with Russian help, could make a test

by the end of this year and be deployed by 2000, according to an Administration official. With a 780-mile range, it could hit Tel Aviv or Riyadh as well as Baghdad.

That's just the beginning. Another Iranian project, the Shahab-4, based on Russia's SS-4, could be deployed in four or five years. It packs a 2,200-pound payload, flies faster to elude defenses, and could reach Europe with its 1,200-mile range.

Under U.S. prodding, Moscow is toughening its stance. Last year, Russia canceled a contract that rocket maker NPO Khimvolodud had with Iran to develop an engine for the Shahab-4. In November, it expelled an Iranian diplomat for trying to steal weapons designs. And on Feb. 18, Moscow published a de-

claration tightening export controls. But just how vigorous enforcement will be is an open question. "You can have better regulations, but a person in the Customs Service still has no incentive to check," says Vladimir Orlov, head of Moscow's PIR Center for Policy Studies.

CASH COW. Russian officials deny that there's a big problem. Space Agency chief Yuri Koptev, for instance, insists that Russia hasn't breached international agreements covering missile nonproliferation.

A Senate subcommittee report in January alleged that Moscow's Polyus Research Institute has supplied guidance

systems to Iran—an assertion the institute's director denies. Also, the report said, Russia's Central Aerohydrodynamic Institute has contracts to help Iran build wind tunnels and provide missile-design software. Meanwhile, Iranian students are studying rocket construction at schools such as Baltic State University in St. Petersburg, according to the report.

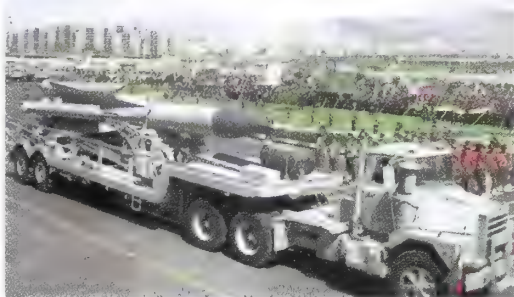
Iran's missile program depends on Russian knowhow. Russian scientists can solve glitches in the development stage, says a U.S. official. So Wash-

ington wants Moscow to restrict the flow of expertise as well.

How much Russia wants to play ball is another question. Exports could be a cash cow for its military-industrial complex, which is, according to Russian news reports, helping Iran develop a communications satellite with potential military uses.

Whatever Moscow eventually does, Tehran will remain an aggressive weapons buyer. Iran, after all, is the only country to be hit by Iraqi weapons of mass destruction. It suffered an estimated 45,000 casualties from Iraq's use of chemical weapons during the eight-year Iran-Iraq war.

*By Stan Crook in Washington,
with Carol Matlack in Moscow*



HOT SPOT: Missiles on parade in Tehran

GLOBAL WRAPUP

LESS SPENDING IN CANADA

Canada has just balanced its budget for the first time since 1970. But Prime Minister Jean Chrétien won't be bragging about the country's sky-high personal income taxes or paying down any outstanding government debt. On Feb. 24, his governing Liberal Party unveiled new budget cuts, chiefly on higher education, that will cost \$7.6 billion through fiscal 2000.

Critics charge Chrétien should pay more attention to debt reduction. The \$18 billion piled up in years of run-

ning deficits puts Canada second behind Italy in debt levels among major countries. Chrétien is offering tax cuts totaling \$5 billion to low-income earners. But he's leaving top income rates at more than 50%—a major factor in Canada's brain drain to the U.S.

GERMAN CORPORATE FLIGHT?

► SGL Carbon Group was a wild success when German chemical giant Hoechst spun it off in 1995. But the company, which specializes in carbon and graphite products, has lost its luster since European and U.S. offi-

cials began ongoing antitrust investigations last year. On Feb. 24, after news that the U.S. Justice Dept. had fined a Japanese competitor for price-fixing, SGL shares fell more than 16%.

Meanwhile, Chairman Robert J. Koehler is hinting that unless Germany reforms its laws on stock options and share buybacks, SGL might move its tiny Wiesbaden headquarters out of the country. Koehler has previously championed shareholder value, but the promise of a share buyback may not pacify investors if Justice hits SGL with a heavy fine.

CEO FITES VOWS
SUSTAINED SALES
GROWTH

STRATEGIES

A NEW CAT ON THE HOT SEAT

Slowing global markets are shaping up as the first big test for the revamped Caterpillar

For eight years, CEO Donald V. Fites has been working to insulate Caterpillar Inc. from surprises. But on Feb. 22, Illinois members of the United Auto Workers gave him a shock. Although union leaders had finally agreed to a contract to end the company's six-year labor standoff, rank-and-file workers rejected the deal.

The setback comes at a particularly

delicate time for the construction and heavy-duty equipment giant. Thanks to booming U.S. markets, a flood of new products, and a hugely successful restructuring that has slashed costs while making global diversification priority No. 1, the Peoria (Ill.)-based company has been on a tear. But with a slowdown in global markets sure to give management plenty of new problems to worry about, Cat had hoped finally to put its bitter labor troubles behind it.

That looks unlikely to happen anytime soon. The union rejection has put an end to talks—and for now, an end to any hope Cat had of being able to hire lower-cost workers at its union plants.

Still, if Cat's managers are worried they're not showing it. Although Fites, 63, wouldn't comment for this article, his executives brush off any difficulties ahead. Overall, the company has "never been in a better position" to weather a tough environment, says Cat Vice-President James W. Baldwin, who oversees the key service and parts business.

IMPORT SCARE. For now, Wall Street also appears fairly sanguine. Cat shares tumbled 36%, to 44, in less than a month last fall after news hit that Asia's currency crisis would trim sales by \$80 million, but they have since recovered to around 52. The reason: Despite initial fears that collapsing Asia



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The Ultimate Corporate Payment System

encies would lead to a flood of cheap products from Asian rivals, it's now clear that most don't have capital to launch an export attack. Manufacturers at Cat "had their stock punished too much" last fall, says Jeffrey P. Davis, chief investment strategist with State Street Global Advisors, which holds 1.5% of Cat's shares.

Of course, that hardly means the market is trouble-free. The U.S. market, where Cat sells 49% of its goods, is expected to slow in 1998. And Asia, its fastest-growing market, is suffering a headline-grabbing downturn. Already, American dealers say barely any new, heavily discounted Cat equipment has begun to trickle into the U.S. from abroad, as customers dump equipment to get cash. The slowdown promises the toughest test yet of the new Cat—the combat-tested CEO has built.

One thing is for sure: The reborn company has rocketed through a downturn with flying colors. Since 1993, when Fites completed its manufacturing overhaul and soaring demand for construction equipment in the U.S. and developing nations, sales have leaped from \$11.6 billion to \$23.9 billion, an average of 13% a year. Meanwhile, earnings have risen a stunning 45% annually, jumping from just \$1.6 billion to \$2.3 billion last year. Investors have also won big: In five years, the stock has more than tripled.

Fites's tumultuous restructuring was in response to a painful industry collapse in the 1980s. Global demand was dropping fast, and the weak yen moved Cat's biggest rival, Japan's Komatsu Ltd., to undercut prices by 40%. When Komatsu began to gain share, Fites—and Cat—got the scare of their lives.

Fites began by overhauling manufacturing in Cat's core truck and tractor divisions. He invested almost \$2 billion to modernize his U.S. plants. New state-of-the-art machinery helped Cat cut a time out of such mundane tasks as painting, for example, and vastly simplified production. Today, Cat can build different models from the same basic design. The changes—together with the increased use of temporary workers in nonunion plants—have also greatly improved Cat's flexibility. The company can now change production levels on a week's notice—down from six months at the height of its 1980s crisis.

Altogether, Cat's manufacturing time has fallen 75%—one key reason operating margins have exploded, from 5.2% in 1993, to 12.6% in 1997.

Faster production has also allowed Fites to slash inventories. Gone are the long order backlogs and dealer inventories that weighed heavily on Cat's books; today, it refuses orders more than three months in advance. At the same time, Cat has broadened its products. In the last two years, it has introduced 90 offerings—some all-new, some well-targeted line extensions. In 1997, for example, Cat introduced a telescopic handler—essentially a tractor with an arm on it that allows masons to work their way up the side of a building.

Good timing helped with the turnaround, too. As the combination of re-

duced costs and the end of recession restored the company's financial health, Fites pushed into new markets. He focused on Asia, where infrastructure development created huge demand. Markets in Latin America, Central Europe, Russia and other former Soviet states.

boost engines to more than 25% of Cat sales. "They are trending toward smaller, easier-to-operate generators," says Siegfried R. Ramseyer, vice-president of Cat Asia. "This we can do very, very well." He says sales could triple in the next few years.

The company's largest acquisition to date—the \$1.3 billion purchase of Britain's Perkins Engines, which closed in February—was directed at another target altogether: the fast-growing \$3.6 billion market for compact construction machinery. These machines, typically operated by one person, are the industry's hottest segment. The star of the category: skid-steer loaders, which break up asphalt, move dirt, and do such a variety of useful things that sales are growing a red-hot 11% a year.

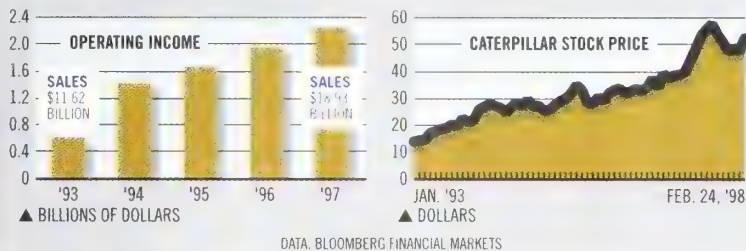
Today, Cat is all but absent in the lucrative small-equipment market, but Fites wants a 20% share by 2003. He's counting on big gains from Perkins, which makes engines for skid-steers. Since engines account for 25% of the costs of a skid-steer, Cat figures that trimming those expenses will allow it to undercut rivals while maintaining margins. But Rivals Deere & Co. and Case Corp. are also revving up. "It is going to be a brawl," says industry consultant Frank Manfredi.

Elsewhere, Fites has tapped other new markets by focusing dealers on rental equipment. Initially unpopular with dealers, who must keep rental gear on their books as assets, the change drew lots of smaller customers. The added demand also helped keep prices strong. In 1997, for example, when few companies could do so, Cat raised prices.

But that, as they say, was then, and this is now. The question today is whether Fites can keep up the performance. Speaking to investors at a Boston conference, he promised sustained sales growth of 5% to 7% annually for the next decade. But outside predictions for 1998 are much lower. Analyst Eli S. Lustgarten of Schroder & Co. expects sales to grow only 3.2% in 1998, to \$19.5 billion. Operating earnings should nudge up only 1.5%, to \$2.3 billion. Although he believes "strategically they are in a very strong position," Lustgarten doesn't expect Cat to avoid the cyclical slowdown. Fites has brought Cat far. But not that far.

By De'Ann Weimer in Peoria, Ill.

CAT IN THE 1990s: FAST GROWTH HAS THE STOCK CLIMBING



duced costs and the end of recession restored the company's financial health, Fites pushed into new markets. He focused on Asia, where infrastructure development created huge demand. Markets in Latin America, Central Europe, Russia and other former Soviet states.

POWER SURGE. Today, some 51% of Cat sales come from overseas—though Fites wants to hit 75% by 2008. To cut the risk of fluctuating currencies—and trim labor costs—Fites has also pushed much manufacturing abroad. Today, roughly half of Cat's 74 plants are abroad, vs. just 39% of its 38 plants a decade ago. In the wake of the UAW's rejection of the labor contract—which will prevent Cat from hiring new workers at lower wages or demanding more flexible scheduling in union plants—analysts say the percentage of foreign production could go even higher.

Fites has also bulked up in less-cyclical businesses like electric power generation. An offshoot of its long-standing engine business, the move into power gained steam in 1996 when Fites purchased a German maker of engines for generators. Driven by demand for power in developing countries—where governments often don't want to build big power plants—generation has helped

COMMENTARY

By Howard Gleckman

YOUR TAXES MAY BE HIGHER THAN YOU THINK

What will your tax rate be this year—15%, 28%, 31%, 36%, or 39.6%? The answer: maybe none of the above. Those are the official rates in the Internal Revenue Service tax tables. But about 33 million Americans will actually pay much higher effective marginal rates.

That's the stunning conclusion of a Feb. 3 study by the congressional Joint Committee on Taxation. The reason: Over the past 15 years, Congress has enacted 23 different tax credits and deductions that phase out as income rises. True, some of these breaks benefit taxpayers who can take full advantage of them. But as they disappear, they begin to have a perverse effect: The tax on the last dollar you earn can rise sharply as the value of your tax benefit falls.

The wealthy are whacked as their personal exemptions and itemized deductions are gradually eliminated. Some 4.5 million high-income taxpayers get hit by hidden rates as their income rises and deductions such as medical expenses, mortgage interest, and state taxes disappear. That means a taxpayer with a top rate of 39.6% really gets clipped for nearly 41%. But the real victims are low-wage families with kids, who lose tax credits as their earnings rise, and middle-class retirees, who are taxed on Social Security benefits if they work.

ANTI-WORK. Lawmakers say all these phase-outs make the code fairer. In truth, they are a quiet way to raise revenue without hiking published rates. And they add complexity to the tax code and discourage hard work and saving. "It's a rotten way



REAL VICTIMS: Those going off welfare take a big hit

to run a railroad," says Robert S. McIntyre, director of Citizens for Tax Justice, a liberal think tank.

Consider this simple example: Say the tax rate for income up to \$1,000 is 15%. That means Jane Taxpayer forks over \$15 on every \$100 she earns. But if Jane is eligible for a 10% credit, her tax is really \$5—an effective rate of only 5%. Now suppose Jane's tax credit declines by one percentage point for each dollar she earns over \$100. So when she earns \$101, her tax jumps from \$5 to \$6.06, and her take-home pay drops from \$95 to \$94.94. Thus, her marginal rate on that additional dollar is over 100%, a powerful disincentive to work for an extra buck.

Perhaps the cruelest real-world example is the mother pushed off

welfare. To ease the transition, she is eligible for the Earned Income Tax Credit to supplement her pay. The EITC allows a working mother with two kids to get an annual payout of about \$2,500—as long as her income remains below \$12,000. But once her income exceeds that level, the EITC and a child-care credit slowly disappear, causing taxes to shoot up. The Joint Committee reports that a mother of two who earns \$25,000 pays an effective marginal rate of 38.5%, not counting payroll taxes. That's

nearly the same rate as that of a married couple earning \$300,000.

For some former welfare moms, it can be absurd. Take an unmarried mother who does just what the family values folks want—gets married and gets a job. Now, she and her husband average about \$6.50 an hour, or a combined \$27,000 a year. An Urban Institute study estimates she will give back 100% of what she earns in the form of higher taxes and lost benefits. Bottom line: She's no better off economically than when she was single and on assistance.

Last year, nearly every tax break enacted by Congress came with tax code sleight-of-hand. Even crazier, all these benefits phase out at different income levels, so you've got to run a separate set of numbers every time you get hit.

These hidden rates are unfair, complicated, and anti-work. Yet Congress—abetted by the President—can't resist sneaking them into the tax code. No wonder the public is so disgusted with the games Washington plays.

*Senior Correspondent
Gleckman covers taxes
from Washington.*

STEALTH TAX RATES

THE WORKING POOR

As wages increase, they lose the benefits of the Earned Income Tax Credit, the child-care credit, and other tax breaks. A single, working mother can pay rates of nearly 40% on each extra dollar earned between \$20,000 and \$30,000.

SENIORS

If they work or earn more than \$34,000 in investment income, up to 85% of their Social Security benefits may be taxed. For some, that can mean almost every penny of that extra income is taxed.

OTHER

THE CLASS

Couples with income exceeding \$124,500 gradually lose the benefits of their itemized deductions. The result: Their true marginal tax rates are one full percentage point higher than the published rates.



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BofA Basher: Plaintiff Buster says the bank "felt it was above scrutiny"

LAWSUITS

BANK OF AMERICA'S BACK IS AGAINST THE WALL

A trial looms over charges that it defrauded local governments

After the Great San Francisco Earthquake of 1906, BankAmerica Corp. founder A. P. Giannini personally lent cash to victims, asking only for a handshake as collateral. Ever since then, the state's largest bank has worked hard to be a model corporate citizen, sponsoring cultural events, boosting minority hiring, and forging close ties with California's political elite. One of the many payoffs has been BofA's role as chief banker for hundreds of cities and counties along the coast.

But now, many of the bank's longtime government customers are accusing the economic and political powerhouse of

thievery. In April, State Attorney General Daniel E. Lundgren, the city of San Francisco, and 250 other political subdivisions will go to state Superior Court in a suit charging the bank with defrauding taxpayers of hundreds of millions of dollars while it managed municipal bonds for them from 1978 to 1993. As the trial draws closer, elected officials are giving the nation's fifth-largest bank a drubbing—one that threatens to drive away some of the bank's valuable clients. "The bank is so entrenched that it felt it was above scrutiny and above the law," says Riverside County Supervisor Bob Buster, one of the plaintiffs.

The suit centers around the bank's role as the trustee for billions of dollars of municipal-bond offerings. This job required BofA to invest money raised by the state and cities and then to forward proceeds to thousands of bondholders. Bondholders were generally required to send in coupons and matured bonds to claim interest and principal, but as many as 3% of them may have failed to do so. The plaintiffs allege that BofA illegally kept the unclaimed money, rather than returning it to the state and cities.

"BAFFLING." The suit also accuses the bank of billing for services it didn't perform, overcharging for those it did perform, and hiding evidence of its alleged misdeeds (table). Arguing that other institutions with bond trust companies have engaged in abuses similar to those BofA is alleged to have committed, Zane Mann, publisher of *The California Municipal Bond Advisor*, hopes the suit will "open the curtain so people can see what's going on" and eventually "close down some of these practices."

Bank of America denies it committed theft, fraud, document destruction, or any of the other illegal acts alleged in the suit. While bank executives admit its corporate trust office made some errors, it claims these mistakes unintentionally arose in the process of switching to a new record-keeping system. Before the suit was filed, the bank says, it conducted an internal review and returned to unclaimed bond money it owed, about \$47 million. In fact, it sold its municipal-bond-management unit in 1995. In the eyes of bank executives, politicians are simply bashing the bank to make hay with voters. "The steady stream of invective aimed at the bank is baffling," says BofA spokesman John Keane. "The more of a media campaign they conduct, the less of a case we think they have."

The controversy might never have

HOW BADLY DID BofA BLUNDER?

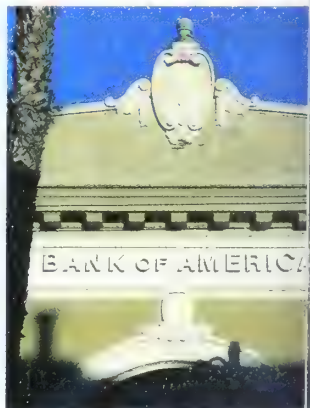
More than 200 California cities charge that Bank of America, which managed their bond offerings, cheated them out of hundreds of millions. Here's what BofA allegedly did:

TOOK MONEY THAT BELONGED TO THE CITIES In the days when bondholders were supposed to send in coupons to get interest payments, many neglected to claim their money. BofA illegitimately kept hundreds of millions in unpaid funds, the governments claim.

DESTROYED EVIDENCE After internal audits revealed that it may have owed money to the cities, the bank allegedly eliminated records of the debts.

OVERCHARGED FOR SERVICES Excess fees were charged for canceling bonds, transferring funds, and maintaining accounts, among other things, plaintiffs claim.

DATA: CALIFORNIA ATTORNEY GENERAL, BUSINESS WEEK



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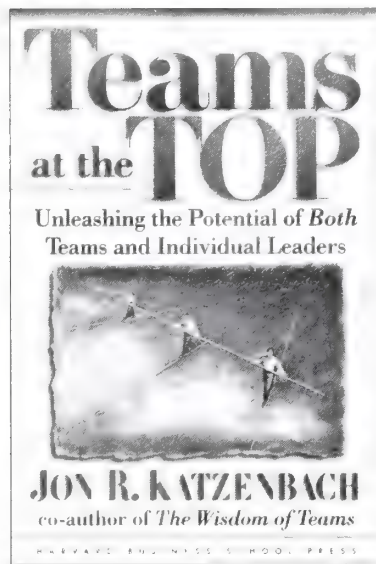
Baylor, University of Pennsylvania and Stanford. Together, we're seeking new ways to help get patients the health care they need. ■ Already, we send timely reminders that encourage members to see their doctors for immunizations to prevent illness and screenings that diagnose disease early enough to do something about it. One result has been a significant reduction in late-stage breast cancer. ■ To better manage chronic diseases, we've created outreach efforts that have reduced asthma emergencies 60%, promoted eyesight-saving laser therapy for diabetics, and improved the quality of life for people with congestive heart failure. ■ There's more work to be done. And we'll do more than our share of it. Because no matter how complex, it has never been our policy to turn our back on a problem. Whether it's that of a patient, or of an entire health care system.



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Legal Affairs

come to light but for a whistle-blower named Patrick Stull. After joining BofA as a systems analyst in 1978, Stull rose to vice-president in the corporate trust division. Although he did not participate in bond management, Stull says he heard rumors "about the mess" and observed some disarray firsthand. "They had boxes and boxes of live bearer bonds lying around, with no security," he says. The bank responds that Stull never complained about these problems while he was a member of management.

Because he needed more time to take care of a seriously ill newborn son, Stull left the bank in 1990 to become a private consultant specializing in advising governments on cash management. Hired by four municipalities that had business with BofA, Stull discovered that the bank had overcharged each city for bond-management services and eventually won each of them refunds.

Convinced the problems were widespread, Stull filed a whistle-blower complaint against the bank in 1995. State law allows citizens who learn of possible wrongdoing that costs the government money to sue—and to keep part of the proceeds if they win. His suit obligated the attorney general's office to conduct its own probe, which uncovered evidence that the bank may have kept unclaimed bond money.

OFF TRACK. Based on their investigation, government officials say BofA's backroom operations were a mess for years, starting with disorganized manual record keeping. By the mid-'80s, the suit argues, the bond office had lost track of the money it had in hundreds of accounts. As a result, the bank did not know if there was enough money in each bond account to pay outstanding claims—potentially a violation of state law requiring bond accounts to be "balanced."

In 1986, the bank changed to a new computerized system, but the conversion, plagued by bad management, never straightened out the accounts, plaintiffs say. According to bank documents, the company that sold BofA the new record-keeping system advised the bank in 1987 that it should figure out how much it had paid out from each bondholder account and what was left unclaimed. But nearly two years later, an internal audit gave the unit an unsatisfactory rating, noting that only 50 of 7,000 bond-issuance accounts had been balanced. BofA General Counsel James N. Roethe could not recall details about the vendor's warning. He says the audits were "self-improvement" attempts to solve the problem.

The plaintiffs claim, though, that the bank started to artificially balance the

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Legal Affairs

accounts, dropping from the system unpaid bonds and falsely recording them as paid. Any cash left over in a bondholder account, they contend, was placed in a "reserve" to pay other expenses. As evidence, the plaintiffs cite several internal BofA documents, such as one indicating that in July, 1991, trust officers were unable to identify the source of \$1.2 million in a customer account. Calling it a "sundry recovery," an executive of the unit transferred it to the bank's own reserves. Roethe says the reserves were used to pay off bondholders who came in with claims.

By the end of 1991, the suit alleged the bank "destroyed or lost" most of the paperwork recording this alleged accounting cleansing campaign—a charge the bank denies. The judge has appointed an expert to help determine the veracity of the records, and Roethe is convinced that

BofA denies that it destroyed records and says the charges mean foes lack evidence

bank will be vindicated. "We have most of the documents or we have some backup form of documentation," he says. The reason opponents are charging document destruction, he says, is because they have not been able to come up with evidence that the bank owes more money. "Frankly, I don't think they have devoted the time or energy to look at the records," says Roethe.

Diane L. Merdian, an analyst at NationsBanc Montgomery Securities Inc., believes that the bank's ultimate liability, if any, will be "in the tens of millions" rather than the hundreds of millions sought by its opponents. But with politicians bashing the bank, there are other worries. "Probably the real economic issue will be whether they can lose business as a result of the appearance of having harmed customers," she says.

That's bad news for an institution that has spent so much time and energy burnishing its image. Unless the parties can reach a settlement soon—at right now, there's no sign that a deal is in the offing—it may be some time before BofA can win back its good name in town halls across California.

By Susan B. Garland in Washington, with Steve Hamm in San Francisco and Mike France in New York

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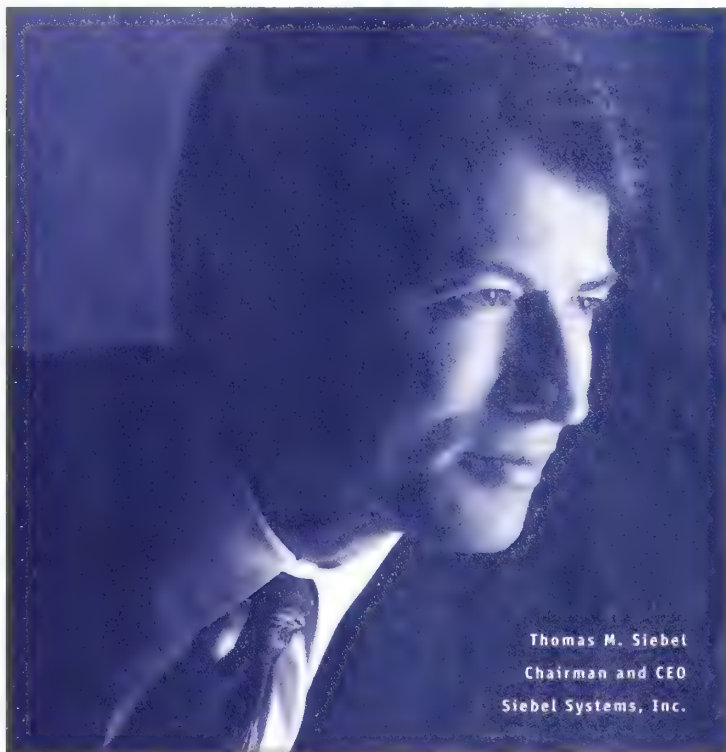
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"I don't know what we'll be serving in the year 2000, but we'll be serving more of it than anybody"

— Ray A. Kroc, founder of McDonald's Corp.

The McDonald brothers' first restaurant, founded in 1937 in a parking lot just east of Pasadena, Calif., didn't serve hamburgers. It had no playground and no Happy Meals. The most popular item on the menu was the hot dog, and most people ate it sitting on an outdoor stool or in their cherished new autos while being served by teenage carhops.

That model was a smashing success—for about a decade. Then America's tastes began to change, and the Golden Arches changed with them. As cars lost some of their romance, indoor restaurants took over. When adults became bored with the menu in the 1960s, a new sandwich called the Big Mac wooed them back. As consumers grew weary of beef, McDonald's introduced bite-size chunks of chicken in the

Can It Regain Its Golden Touch?

Cover Story

early '80s and within four years was the nation's second-largest poultry seller.

The changes were vital, but never radical. McDonald's gave us what we wanted before we even knew we wanted it, whether it was movie tie-ins or Egg McMuffins. Along the way, it built one of the world's best-known corporate icons and its most ubiquitous store. The philosophy was neatly summarized by Ray Kroc's brash vow: whatever people ate, McDonald's would be the ones to sell it.

But now, two years shy of Kroc's benchmark for the far-off future, that goal seems less assured than ever. Forget for a moment all the recent talk about Burger King Corp. and Wendy's International Inc. stealing customers from McDonald's. With a 42% share of the U.S. fast-food burger market, McDonald's still easily outpaces its rivals. Nonetheless, the problems under the famous Golden Arches are far more serious than a failed Arch Deluxe here or a french-fry war there. Quite simply, McDonald's has lost

of its relevance to American culture—a culture that it, as much as any other corporation, helped to shape. Not a still booming international dividend responsible for half of sales and 60% of profits, can mask the troubles.

The company that once seemed a half-century ahead of pop culture today is unable to construct even an appealing new sandwich. Its last successful new product was the Chicken McNugget, launched in 1983. In the '90s, the company has careened from tests with and veggie burgers to confusing promotions such as last year's Cam-55. Earnings in 1997 inched up 4%, to \$6 billion, on sales of \$11.4 billion, a 1% increase. That's well below projections McDonald's itself made a few years ago.

For a company that enjoyed sizzling growth for five years based on its ability to read and shape popular trends, the breadth of its problems is astonishing. Since 1987, McDonald's share of fast-food sales in the U.S. has slipped almost two percentage points, to 16.2%. The drop has come as the company has increased its number of restaurants 50%, far outpacing the industry's expansion rate. The restaurant's domestic sales have climbed only 18% since 1989, while operating profits haven't even kept pace with inflation. Profits have risen just 2% a year in that period. That trend has eroded U.S. per-store profits by 20% since 1989—or a huge drop after inflation. Meanwhile, nearly every other top consumer brand, from Disney to Marlboro, has prospered.

Menu Tweaking. McDonald's has chalked up that dismal performance despite the fact that it owns one of the best known brands on the globe. The company has been unable to harness the strength of its brand to grow beyond its basic formula of burgers and fries. During a period when Americans have abandoned their kitchens in droves for food cooked elsewhere, the Golden Arches—easily the world's largest purveyor of prepared food—has failed to

adapt. It's as if hundreds of thousands of people started drinking soda for breakfast and Coca-Cola Co. wasn't benefiting. McDonald's has totally failed to adapt to its original concept," says Sirhan C. Williams, chairman of the consulting group, a New York-based consultancy that works with consumer companies.

Now, McDonald's is embarking on a major effort at reform. Last year, Chief Executive Michael R. Quinlan shuffled his U.S. management team. He replaced the decentralized structure with a more centralized one. The company's entrepreneurial spirit is being replaced by a new cooking system set for 2000 that will make it easier to customize sandwiches, improve quality, and expand the menu. Fundamentally, however, McDonald's won't be much different. "Do we have to change?" asks Quinlan. "No, we don't have to change. We are the most successful brand in the world."

McDonald's, though, is doing some tinkering. The new head of the domestic division—Jack M. Greenberg, a pleasant 54-year-old lawyer who has been with the

Where's the Sizzle?

Stock performance of the world's top six brands

BRAND	2-YEAR TOTAL RETURN
COCA-COLA	71%
EASTMAN KODAK	-8
GILLETTE	101
MCDONALD'S	3
SONY	49
WALT DISNEY	78
S&P 500	63

DATA: INTERBRAND, BLOOMBERG FINANCIAL MARKETS

company 16 years—has brought in a handful of new managers, including executives from Burger King, Boston Market, and General Electric Co. "We are not afraid to do things differently," Greenberg says. In a first for the burger giant, McDonald's in February bought a stake in another restaurant, a 14-outlet chain in Denver called Chipotle Mexican Grill.

But executives emphasized that the heart of the company's menu will remain the same—and that it believes it can squeeze new profits from the U.S. burger business, even though McDonald's already dominates the crowded segment. "We will extend our line, rather than going in more radical, different directions," says Quinlan, 53, who started in the company mailroom at age 19. "I'm a fan of menu tweaking."

Compare the McDonald's strategy with that of other companies that have prospered despite wrenching changes in their industries. When GE realized that manufacturing had become less profitable, it moved into financing. When Walt Disney Co. found it hard to lure more people to its theme parks, it built hotels and captured more dollars from the tourists already there.

And Coca-Cola spun off its bottling business and focused instead on becoming a marketing powerhouse. The

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DESPITE A MASSIVE EXPANSION...



DATA: MCDONALD'S CORP., TECHNOMIC INC.



Top executives seem to be in denial as Mickey D's performance has deteriorated

difference is profound: If McDonald's had added shareholder value at the same rate as Coca-Cola over the past ten years, its shares today would be worth \$170 each. Instead, they bring less than \$55.

FAMILY VALUES. By contrast, McDonald's core recipe has changed little since the early '80s. "McDonald's needs to move the question from 'How can we sell more hamburgers?' to 'What does our brand allow us to consider selling to our customers?'" says Adrian J. Slywotzky, a partner at Corporate Decisions Inc.,

Cover Story

a consulting firm in Cambridge, Mass.

Such sweeping vision will not come easily. McDonald's is one of the nation's most insular large companies, with a management team more typical of a private company than a global powerhouse. The average top executive started working at the company when Richard Nixon was President. The 15-member board of directors has sat out the corporate-governance revolution and is more than two-thirds filled with current and former executives, vendors, and service providers (page 76).

As the company's performance has deteriorated, top executives have tended to blame others. They have publicly blasted dissident franchisees, whom they dismiss as a small faction. Negative news accounts are chalked up to misperceptions by reporters. And one persistently critical Wall Street analyst—Damon Brundage, now at J.P. Morgan &

Co.—was barred from the company's latest biennial briefing.

And while some companies, such as IBM and AT&T, have brought in outside leaders—albeit reluctantly—to help guide management as the business changed, McDonald's has largely clung to the "McFamily" philosophy of the 1950s and 1960s, which rewards managers who start young and stay for life. Headhunters, noting that virtually no alumni from the McDonald's Oak Brook (Ill.) headquarters can be found running other companies, say it isn't where they look for talent. "They are no longer the beacon of great success they used to be," says a Chicago-area recruiter.

Wall Street seems to share that sentiment. Over the past two years, while the Standard & Poor's 500-stock index grew by 63%, McDonald's shareholders could have made more money in an insured savings account. Had you invested \$100 in the company two years ago, you'd be holding \$103 today. Of the world's 10 most powerful brands, as ranked by Interbrand, a New York consultant, only beleaguered Eastman Kodak Co. has had a worse run over that period (table, page 71). Shareholders of Gillette Co., meanwhile, have more than doubled their money.

"NOT HOLDING THE PAST SACRED." Even some investors who still believe in the brand are concerned. Davis Select Advisors, with \$500 million in McDonald's stock, has been a shareholder since 1994 on the strength of the company's international operations, but the big investor believes there needs to be changes in management and in the business. "It means not holding the past sacred," says Chris Davis,

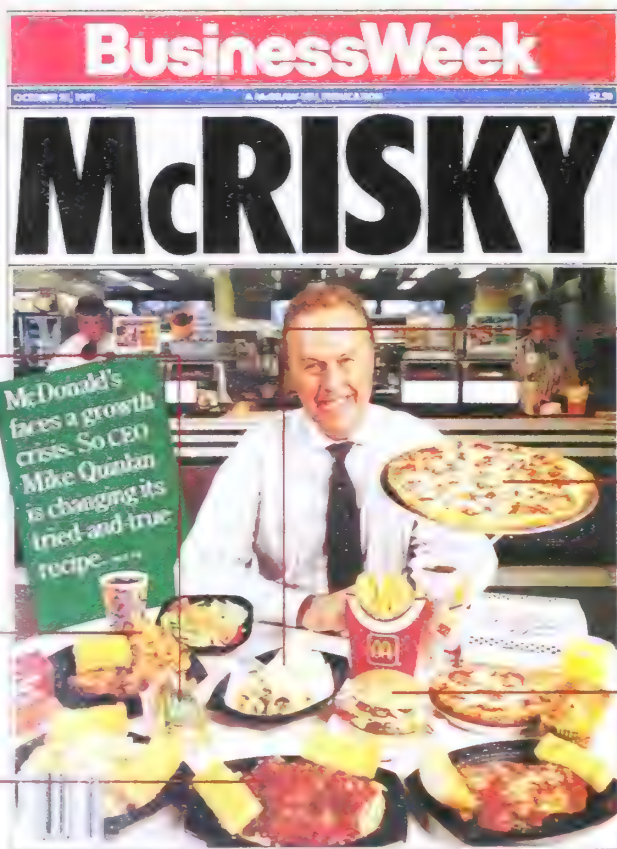
FLOPS

In 1991, BUSINESS WEEK chronicled the millions McDonald's was pouring into experiments. Today, most of those items are off the menu

CARROT STICKS Still available as an optional item in some U.S. restaurants.

FRIED CHICKEN This was on the menu in much of Asia, it's off the menu in the U.S., along with the corn on the cob that came with it.

PASTA McDonald's tried the old favorites, spaghetti and lasagna, with garlic bread. Neither is available anymore in the U.S.



FAJITAS The McDonald's version of this popular Mexican dish never took off, though it's still available in a few U.S. restaurants.

PIZZA The company devoted an entire annual franchisee meeting to talking up this fast-food favorite. Pizza survives in Canada, but it is no longer offered in the U.S.

McLEAN DELUXE This low-fat sandwich debuted in 1991 to woo health-conscious customers. It was erased from the menu in 1996.



After preschool, when they are whiny and hungry, we go there //

— JULIE LAKE

Lake's daughters, 5-year-old Evan and 3-year-old Chloe, enjoy Happy Meals in their Austin (Tex.) home.

olio manager. "There needs to be a sense of urgency." When McDonald's formidable international business faces serious challenges. On the plus side, operating earnings more than doubled in the past five years, and some emerging markets will soon see economies of scale. Says R. Cantalupo, who runs the division: "We're nowhere any kind of penetration that I think is possible."

At the easy markets have been tapped. Now, McDonald's is expanding beyond the bustling Londons and Moscows. As margins are dropping—from 20.5% in '94 to 19.1% last year in overseas company-owned outlets. In each of the past two years, McDonald's has badly missed its projection of 18% to 20% for international earnings growth, falling short of 15% per year after accounting for currency fluctuations. In the fourth quarter, key markets such as Germany and Japan underperformed, largely because of local economic troubles and a strong dollar. Overall, says analyst Dean T. Haskell of Prudential Securities Inc., McDonald's international story is

not quite as good as McDonald's would have you believe."

And the Archers' domestic woes raise a troubling question for the overseas operations: If McDonald's cannot respond to changing market forces at home, how will it adapt over time as its most important overseas markets mature? "It's hugely problematic," Slywotzky says. "If the same set of conditions duplicate themselves abroad, then you have a dead end waiting to happen."

Of course, the strength of the McDonald's brand gives it opportunities to avoid that dead end. Thanks to the movie tie-in trinkets that it gives away, for example, McDonald's is hugely popular with kids. Imagine, says Slywotzky, if it used low-margin burgers to sell a line of high-margin toys—instead of vice-versa. McDonald's says that's not its core business. But the point, says Slywotzky, is that it needs to worry less about market share and more about new profit vehicles.

First, though, McDonald's needs to address an even more fundamental problem: the quality of its

“Do we have to change? No, we don't have to change. We have the most successful brand in the world”

— MICHAEL QUINLAN,
Chairman & CEO,
McDonald's Corp.



“A cheeseburger and french fries will kill me for the day”

— STEPHEN CHAR

The 31-year-old scientist opts instead for Mideast lunch fare that he buys from a food counter inside a Texaco station

food. While the burger giant focused on building more stores, consumers have decided they want better food and more variety. Consumers who eat fast food at least once a month say that both Wendy's and Burger King offer better-tasting fare, according to a recent BUSINESS WEEK/Harris Poll. And in a soon-to-be-released survey for *Restaurants & Institutions* magazine in which

Cover Story

2,800 consumers graded chains based on the taste of their food, McDonald's ranked 87th out of 91—just behind Hooters. “We clearly think we have to do some things with our menu,” says Greenberg, who believes the new cooking system will be a turning point.

The fact is, convenience is no longer enough. In the Harris Poll, more than 90% of consumers listed both taste and quality as “very important” factors in their choice of a restaurant, while location and speed were selected by barely half. Why? With an abundance of choices, consumers no longer choose McDonald's just because there's one around the corner. And with new entrants offering ethnic fare, vegetarian menus, and fully stocked salad bars, fast food no longer has to mean fried food.

KIDS' PLEAS. Take Stephen J. Char, a 31-year-old government scientist in Denver. He has cut his trips to McDonald's in half over the past few years. “A cheeseburger and fries will kill me for the day,” he says. He's found tastier options near his office for about the same price: a taco restaurant, a German deli, and even Haji Babba's—a food counter at a Texaco station that serves stuffed grape leaves.

Even some regulars say it's not the food that keeps them coming back. Julie Lake is the Austin (Tex.) mother of 3-year-old Chloe and 5-year-old Evan. “After preschool, when they are whiny and hungry, we go there,” she says, adding that she rarely eats the food herself. That's bad news for McDonald's, which has had little luck creating dishes that appeal to grown-ups. Last year's Arch Deluxe, though still on the menu, is hardly a blockbuster. As their kids move beyond the Ronald McDonald years, baby boomers like Lake will need a new reason to visit the Arches.

All the while, McDonald's has concentrated on adding restaurants, angering store owners and cutting into margins. It began a major U.S. expansion in the early '90s, even as business was slowing.



“We clearly think we have to do some things with our menu”

— JACK GREENBERG, Chairman & CEO, McDonald's USA

“They built a whole bunch of new stores in the wrong places,” says Dick Adams, who heads up a group of concerned franchisees.

That single-minded focus left a huge opportunity for new competitors eager to take advantage of changing eating habits. In the same nine years that McDonald's U.S. profits have stagnated, Starbucks Corp. has become a \$1 billion company. Supermarket sales of prepared food have doubled, and the “casual dining” segment has emerged. In fact, Americans now spend more on prepared meals sold at delis, supermarkets, and casual dining restaurants than

as Applebee's International Inc. than they do at burger chains, according to Technomic Inc., a market-research firm based in Chicago.

Even among burger chains, McDonald's is no longer the shrewdest innovator. Burger King has nibbled at McDonald's market share with better-tasting burgers. Wendy's has used its new stuffed pitas and spicy chicken sandwich to drive it toward 21 months of sales gains in existing outlets. Carl's Jr., a 708-restaurant chain based in Anaheim, Calif., has opened a Mexican eatery called Green Burrito within 120 feet of its stores. That has helped boost the typically slow dinner business and led to a \$250,000 revenue jump in some stores.

It's not that McDonald's hasn't made a stab at new products. The past decade has seen an array of test products, such as pasta, fried chicken, and fajitas. But customers have been unimpressed, and McDonald's invariably has returned to its core menu. It pulled the plug in 1995 on one of its most interesting ideas, a one-store test of a Boston Market-like chain called Hearth Express, saying it wanted to focus on

McDonald's focus on adding restaurants angered franchisees and cut into margins



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Wall Street analysts struggling to evaluate

building more hamburger restaurants. "The brand expectation, at least until now, hasn't been as broad [as it could be], and that's been an issue for us in the U.S.," Greenberg says. "When you try to sell something that doesn't necessarily fit people's expectations for the Golden Arches, you have a very difficult time." Analysts, however, say that too often the new products just didn't taste good.

The company's recent stake in Chipotle could be a sign that McDonald's is considering new ways to leverage its brand.

Cover Story

Chipotle's fresh, inexpensive burrito wraps are precisely the type of food that has drawn consumers away from the Arches in recent years. Executives have said that they would like to eventually expand and franchise Chipotle, though they caution that the investment, estimated to be less than \$15 million, is far too small to have any impact soon.

WHITEWASH? More significant than the Chipotle venture is McDonald's management reorganization of last summer. Quinlan nudged Edward H. Rensi, who formerly was head of the domestic division, into early retirement and replaced him with Greenberg, who franchisees say is easier to talk to. Five new regional division chiefs, whose territories divvy up the country, now report to Greenberg. The idea: create smaller companies within the larger McDonald's that will recapture its earlier entrepreneurial zeal.

But even the shuffling shows signs of McDonald's discom-

fort with change. Of the five new division heads, none has set up shop outside the Chicago area, and only one has immediate plans to do so. The majority of franchisees still report the same person. The reorganization, charges EVEREN analyst Haskell, "is an effort to whitewash the public by trying to convince Wall Street things have changed when they haven't." Says one investor who manages more than \$1 million in McDonald's stock: "The changes were an improvement, but I don't think it's a dramatic improvement."

One of the most troubling signs of McDonald's unwillingness to grapple with underlying problems is its reaction to outside critics. Greenberg has dismissed the Consortium, a San Diego-based group of franchisees unhappy with the company's direction, as "eight people and a guy with a fax machine."

Adams, a former McDonald's owner who runs the Consortium, claims membership of 300 but refuses to release a list, saying franchisees fear reprisals. But other evidence indicates that unhappiness is more widespread than Greenberg's comment suggests. In a 1997 internal survey, only 28% of franchisees said they thought McDonald's was on the right track. The controversial push to put up more stores remains a flashpoint for many. Says one former operator who claims new stores helped to put him out of business: "Ray Kroc once told me, 'If you work hard, you get treated fairly.' But the guys don't care about the operators."

The media also get blamed for McDonald's bad news. During a guest lecture at Northwestern University's Medill School of Journalism last year, chief McDonald's spokesman

THEY DON'T BITE THE HAND THAT FEEDS THEM

Coca-Cola Co.'s largest customer is McDonald's Corp. Sonnenschein Nath & Rosenthal has been the hamburger chain's lead law firm for decades. DDB Needham Worldwide Inc. and Leo Burnett Co. are two of its longtime ad agencies. And Dean Foods Co. supplies the Arches with pickles.

What else do these firms have in common? Each has an executive, retired executive, or director on the McDonald's board. In fact, by current standards of corporate governance, only 4 of McDonald's 15 directors can be called independent—meaning they don't work for the company, do outside business with it, or have a McDonald's exec sitting on their own board.

"NOT EVEN CLOSE." That's not all: Cross-directorships, in which directors serve on each other's boards, are common, too. Gordon C. Gray, for example, chairman of a Canadian mining company and an independent director, also sits on the board of a subsidiary of Stone Container Corp., a McDonald's packaging supplier whose CEO, Roger W. Stone, is a fellow McDonald's director.

Thanks to pressure from shareholders and regulators, Corporate America

over the past decade has raised the quality of its boards and increased its directors' accountability. But that trend has passed McDonald's by. "They are not even close to keeping up with corporate-governance standards that most

A CLOSE-KNIT GROUP

Along with five current or former executives, McDonald's 15-member board is packed with directors who have links to the company and each other. At right, their ties and the year they joined the board

DATA: BUSINESS WEEK.
McDONALD'S CORP.



HALL ADAMS JR., 64, former CEO of Leo Burnett & Co., a McDonald's ad agency (1993)

GORDON C. GRAY, 70, a Canadian mining executive; sits on another board with Stone (1982)



DONALD R. KEOUGH, 71, former president of Coca-Cola Co., a major McDonald's supplier (1993)

ENRIQUE HERNANDEZ JR., 42, CEO of California-based provider of security guards (1996)



DONALD J. LUBIN, 61, former CEO of McDonald's Chicago Inc. (1967)

TERRY L. SAVAGE, 42, Chicago-based television and print journalist (1990)

Company's prospects say they have largely been frozen out

les Ebeling lashed out at reporters. Ebeling dismissed as "shit" a story in *The Wall Street Journal* that prophetically detailed the problems with Campaign 55, a complicated joint promotion. Then he called *Crain's Chicago Business*, expected weekly that had run critical stories on the company, "a scandal sheet" with a "corrupt" editor. Ebeling says remarks, reported in *Rolling Stone* magazine, were taken out of context.

ABSOLUTELY BAFFLING. Indeed, after eight years in which domestic operating profits have actually fallen, the head marketing for McDonald's USA says the biggest problem the brand is the media's view of it. "If there were one I would want to change about McDonald's," says Senior President Brad A. Ball, "it would be to correct the misperceptions and perceptions that have become so pervasive in the last few years."

Wall Street analysts struggling to evaluate the company's prospects say they, too, have largely been frozen out. They say McDonald's is the only big company they follow in which executives, including Quinlan, refuse to meet with them. "It's absolutely baffling," says Howard Penney of Morgan Stanley, Dean Witter, Discover & Co., one of four analysts who identifies as knowing the most about the company. "Here we are trying to educate people about what we know about the company, and the top management guy won't talk to us." Quinlan says he's in touch with Wall Street. Through it all, he and other executives maintain that the company remains strong. Quinlan has cut his projections for

future growth but still predicts a doubling or near-doubling of earnings per share over the next five years—which analysts call feasible, if optimistic. "In the U.S., we've made some mistakes," Quinlan acknowledges, but he says: "Our greatest days lie ahead."

So what's the problem? Simply put, it's hard to dismiss a lagging stock price, the end of growth in domestic profits, missed international projections, and a decade's worth of failed initiatives. This much is clear: The world's most successful restaurant company is far from achieving its potential—and may be sowing the seeds for further disappointment down the road.

It doesn't have to be that way. Imagine the possibilities: The company uses its powerful brand to figure out a way to grow in its own backyard. The new kitchen production system allows executives to think more broadly about high-quality menu additions. Domestic earnings no longer drag down international growth but add to it. And overseas markets, upon saturation, have a model for future growth.

Of course, doing all that requires thinking about the business in fundamentally new ways and refusing to be tied to the past. It wouldn't be the first time for McDonald's. After all, consider where the Golden Arches would be now if its first owners had insisted on keeping hot dogs as the centerpiece of the menu.

By David Leonhardt in Oak Brook, Ill., with bureau reports



that size, it's stunning." The Association of Corporate Directors recommends "a substantial majority of a company's directors be independent" and many shareholder groups push for cross-directorships; government experts say they can lead directors out for each others' interests rather than those of shareholders. Ebeling denies that the many re-

lationships between its board members and the company are a problem. "We have always had a board that was fairly heavily peopled by inside directors. I am not troubled by that at all," says CEO and Chairman Michael R. Quinlan. He argues that insiders bring detailed knowledge of McDonald's to the board. And director Robert N. Thurston, a former Quaker Oats Co. executive, calls it an active board that "can stick our noses anywhere we want to." To suggest that directors are hampered by company ties "discounts the independence and the pride and the intelligence and the fortitude of the people on the board," he adds.

the type of broad experience and objectivity that a company facing a watershed requires. Despite the hamburger chain's lackluster performance in the past few years, its board has done little to agitate for change, say people who follow the company. "This board is so stale, it's hard to imagine it asking the right questions," Bennis says. Or, as one major shareholder puts it: "If McDonald's is one of your largest customers, I don't think you're going to challenge the CEO too much."

Compare the McDonald's board with those at another globally branded company. Nine of Coca-Cola's 13 directors are independent. The board includes former Senator Sam Nunn, former baseball Commissioner Peter V. Ueberroth, former Delta Air Lines CEO Ronald W. Allen, and superinvestor Warren Buffett.

In fact, inspect almost any company with a brand similar in strength to McDonald's, and you will find more outside directors, a shorter average term, a younger board, and greater diversity of experience. Inspect McDonald's, on the other hand, and you will find a disproportionate number of directors who rely on the company for one kind of paycheck or another.

By David Leonhardt in Oak Brook, Ill.



J. EDGAR HOOVER, 68, director of the Federal Bureau of Investigation (with Don Fred and Dean Witter) is a shareholder.



ROGER W. STONE, 63, CEO of Stone Container Corp., a McDonald's supplier that also owns stake in supplier of take-out bags. Jack Greenberg, president of McDonald's USA, sits on Stone board (1989)



E. BLAIR VEDDER JR., 73, former COO of agency that became McDonald's lead ad agency (1988)

ROBERT N. THURSTON, 65, Former Quaker Oats executive (1974)

Planning for the Unthinkable with GAB Robins

GAB ROBINS NORTH AMERICA HELPS CLIENTS RESPOND TO DISASTER

Disaster, either natural or man-made, is every executive's worst nightmare. The importance of having a catastrophe claims processing system in place cannot be underestimated, says GAB Robins' Hart Hubbard, director of catastrophe services. And Bill McLellan, who heads up GAB Robins Environmental, a wholly-owned subsidiary, adds that the next step, recovery, requires experience and expertise as well. Below, the two talk about how to avoid potholes on the road to recovery.

Q: What is a disaster?

Hubbard: Sudden events that no business model can predict or prevent. Disasters can be natural, such as hurricanes, tornadoes, floods, hail storms, and earthquakes. Or, they can be man-made, such as oil spills and chemical plant explosions.

Q: How have disaster response strategies changed?

McLellan: Today, executives realize that stepping forward and accepting responsibility is in the company's best interest. When disaster strikes, the level of responsiveness can prevent lawsuits or minimize their impact.

Q: So what does GAB Robins do to meet this new, higher standard of disaster response management for clients?

Hubbard: First, we extensively research each client's post-catastrophe needs.



Hart Hubbard,
director of
catastrophe
services for GAB
Robins North
America, Inc.



Bill McLellan,
president and
chief operating
officer of GAB
Robins Environ-
mental, Inc.

We look at their business, their insurance strategy, and the solutions they already have in place. Then, we create a disaster response plan.

Q: How much experience does GAB Robins have in disaster response?

McLellan: The affiliated companies of GAB Robins have been leaders in catastrophe response since 1885. In the 1990s we've been heavily involved with the complex claims resulting from such events as the World Trade Center bombing, the Northridge earthquake and oil spills in Texas and along the Pacific coast. Today, we are helping clients process the surge in claims related to the severe ice storms that plagued the northeast in mid-January.

Q: Many companies already have a disaster response plan. How does GAB Robins make a difference?

Hubbard: Often, executives feel they are prepared. They develop a written plan and they perform drills. But there is chaos when an event happens, because it is not like a drill. We want to instill confidence in our clients, so that when a disaster happens all they have to do is pick up the phone and call us. We will take care of the disaster so they can return to the task of doing business.

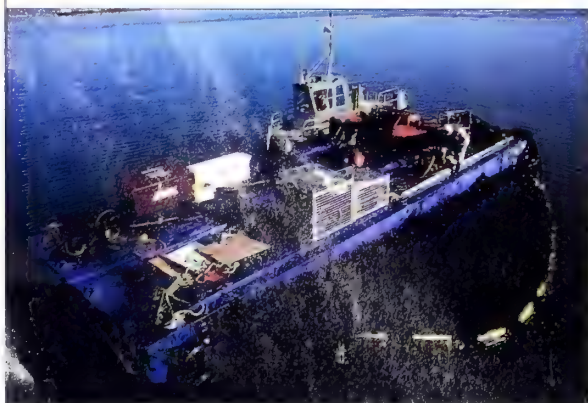
Q: In a disaster situation, logistics can be a nightmare. What systems does GAB Robins have in place?

McLellan: We decide before the disaster when, where, and how money is dispensed to claimants. When disaster strikes, GAB Robins can instantly get a toll free number in place for claimants to call. We can provide claims management support people, office space, software, professional adjusters, energy, and supplies. Organized correctly, recovery from a negative event can actually improve corporate image, if the company demonstrates that it is civic-minded and concerned about individuals.

Q: Many companies worry about the recovery costs. How does GAB Robins help?

McLellan: For environmental disasters, we know what a cleanup should cost. We provide quantitative and qualitative analyses to make sure cleanup costs are consistent with industry standards. With weather catastrophes, Hart's group keeps costs down by getting a claims office up quickly while damages can be best assessed and fraudulent or overstated claims minimized and by using adjusters qualified to handle specific types of storm claims.

Clara Van Hast, a New York-based writer reports frequently on insurance and risk management.



Barge skimming oil after the October 1996 spill in Cape Mohican in San Francisco.

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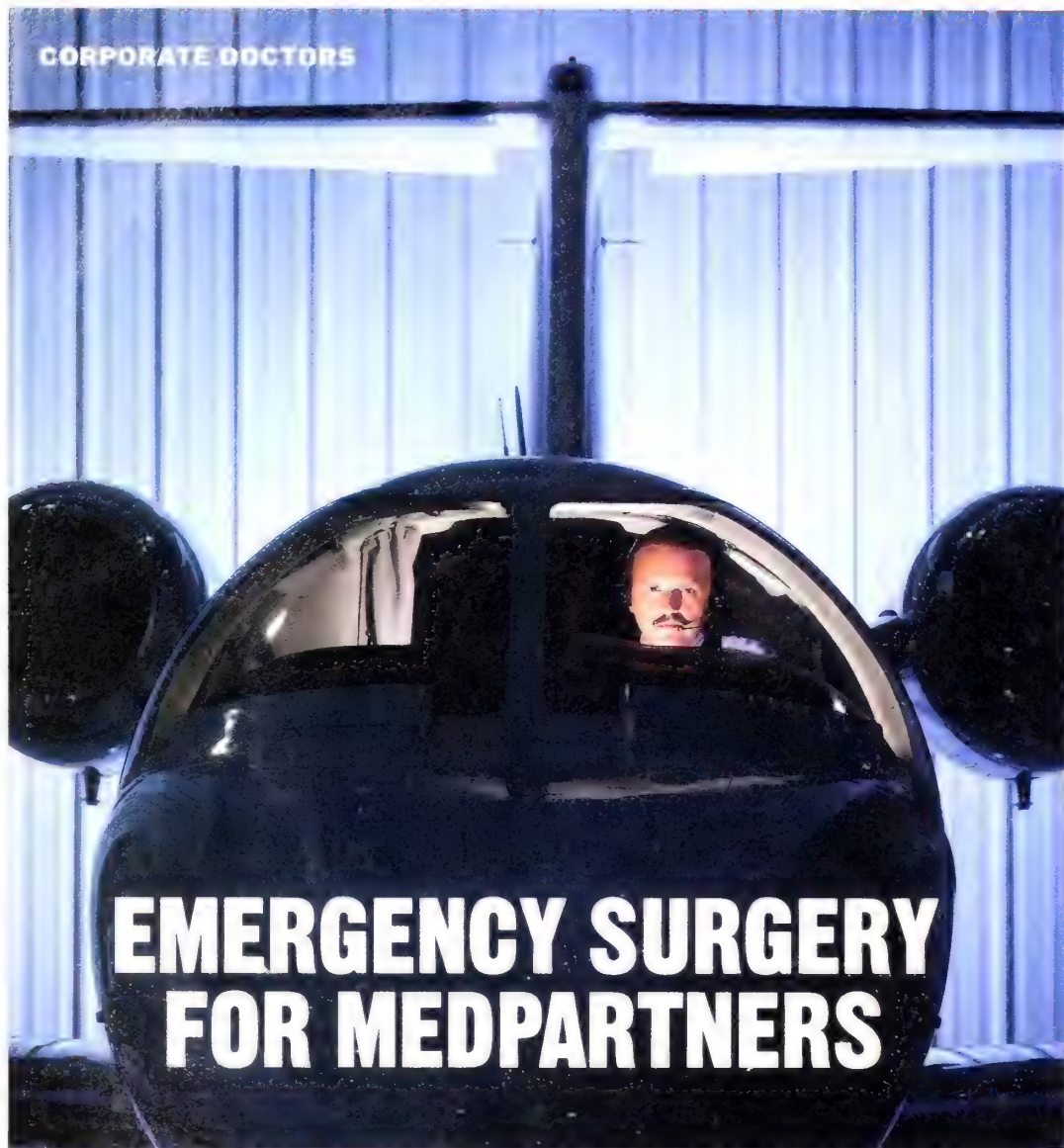
2) MAKE SURE
YOUR CLEANUP DOLLARS
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GAB Robins' response to an environmental crisis begins long before an event ever occurs. Thorough preparation (such as conducting "mock spills" with our clients) allows us to identify potential problems and develop the best response plan. And our environmental experts don't just manage claims; they audit expenses to make sure your cleanup dollars are well spent. Questions? answers@gabrobins.com or call 888.888.4242

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CORPORATE DOCTORS



EMERGENCY SURGERY FOR MEDPARTNERS

Can HealthSouth CEO Scrushy run his company and save MedPartners at the same time?

For Richard M. Scrushy, running one multibillion-dollar health-care company just isn't enough, it seems. The 45-year-old founder and CEO of fast-growing HealthSouth Corp. is also taking charge of MedPartners Inc., a troubled physician-management company that he helped launch. Now, since becoming CEO at MedPartners in January, he has been working overtime in a mad scramble to keep up with his two demanding jobs.

Two CEO titles at once? In this case, it may make sense. A MedPartners

board member since its founding in 1993, Scrushy (rhymes with sushi) has close ties to the company. Earlier this year, he backed a \$6.3 billion merger with rival PhyCor Inc. But PhyCor pulled out of the deal the same day MedPartners announced that a \$145 million restructuring charge would drag 1998 earnings down 30% below estimates. That sent MedPartners stock price plunging by half.

On Feb. 24, though, MedPartners shares soared 14% amid rumors that it would merge with HealthSouth. Scrushy calls the rumors "absolutely not true." Speculation also swirled that Scrushy would sell MedPartners \$1.8 billion pharmacy benefits company or soon name a new CEO.

Scrushy insists he will remain CEO for at least another 90 days. And whatever happens, Scrushy will clearly be

at the center. Both HealthSouth and Scrushy are MedPartners shareholders and have money riding on a turnaround. The aborted PhyCor deal would have netted HealthSouth \$38 million and another \$2 million for Scrushy personally. Instead, he finds himself in the difficult position of fixing MedPartners following the departure of its CEO and Scrushy's longtime friend Larry R. House.

For both MedPartners and HealthSouth—which have shared several directors—Scrushy is the obvious choice to take the reins. The company was formed when House left a top job at HealthSouth to jump into the fast-growing business of physician practice management. And Scrushy backed the venture by putting up a good chunk of the startup money. MedPartners' directors are counting on Scrushy's record: bundling hundreds of small facilities, he has built HealthSouth into a hugely successful outpatient-rehabilitation chain. Turning around MedPartners, which has stumbled in its acquisition-led growth spurt, will require many of the same skills. "[It] is an enormous integration job," says Charles Newhall, a member of both boards. "But Richard has proven he can do that at HealthSouth."

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People

Stephen F. Wiggins stepped down as chairman of Oxford Health Plans Inc. as the HMO veered into financial straits following years of torrid growth.

The problems at MedPartners have some investors wondering whether the overlapping boards have done their job. "The board has not done its duty to make sure it was adequately informed," says Jack McGowan, a portfolio manager at Clover Capital Management.

Scrushy insists he had no clue about the extent of MedPartners' problems before the PhyCor deal collapsed. "All I knew is what was presented to the board," he says. And he asserts he can quickly fix the problems before turning MedPartners over to a new CEO. Many investors agree. Portfolio manager Pedro Verdu of AmSouth Bancorporation in Birmingham, Ala., doubled his stake to 300,000 shares on news of Scrushy's appointment. "This is the best

thing that can happen to MedPartners," says Verdu.

Those who work with Scrushy say he drives his troops hard and is obsessed with the smallest details. He once insisted that an executive leave a meeting be-

cause his necktie wasn't on straight, according to one HealthSouth director. Scrushy denies that but concedes he is demanding because he has set such high goals. "Fear is good," he says. "It motivates people."

Scrushy wants HealthSouth to become nothing less than the Wal-Mart or the Coca-Cola of health care by providing a wide range of services in any of HealthSouth's 1,800 facilities. A back patient, say, can get an X-ray and undergo surgery at one outpatient facility, then receive massage therapy at one of HealthSouth's rehabilitation centers. "Patients should be able to get consistent treatment no matter what part of the country they're in," he says.

Impeccably dressed and manicured, with a diamond-studded watch and diamond ring, Scrushy is as zealous about details at home as he is at work, says his wife, Leslie, his former assistant. And Scrushy immerses him-

RICHARD M. SCRUSHY

BORN 1952, Selma, Ala.

EDUCATION B.A., University of Alabama, 1974.

CAREER

1974-77 Teaches respiratory therapy at University of Alabama.

1979-83 Climbs up the ranks of hospital chain LifeMark, to vice-president and general manager.

1984 Found HealthSouth, an outpatient-rehab business.

1997 Acquires competitor Horizon CMS in \$1.7 billion deal.

1998 Named CEO of MedPartners, charged with fixing the troubled physician-management company.

MANAGEMENT PHILOSOPHY "Fear is good. It motivates people."

FAMILY Twice divorced and recently remarried to his former secretary, Leslie. Six children from his previous marriages.

INTERESTS Flying, fishing, country-and-western singing.

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the routine of raising his six children from two previous marriages—four of them live with them. "Having worked for me, I would've never believed how important his family is to him," she says. "I've never seen him lose time, Scrushy even pilots his own jet."

That jet will come in handy as he flies around the country to clean up the mess his buddy Larry House left behind at MedPartners. The huge write-off came as a complete surprise, angering Wall Street and speeding House's departure. Scrushy hasn't gone far. House now works for Scrushy's venture-capital firm just outside the hall in HealthSouth headquarters. Stepping down, House says, "was the right thing to do."

KEEP YOUR JOB. The pair remain friends, though House's departure from MedPartners marks a difficult fork in the road for a highly productive team. Their friendship dates back 25 years, and the two were respiratory therapists in a local Selma (Ala.) hospital. Scrushy got the job through his mother, and House, who also introduced House to his son, Scrushy went on to enroll in the University of Alabama at Birmingham, where he got a degree in respiratory therapy. After graduation, he went to work for a non-profit hospital-management company, LifeMark Corp.

With the for-profit health-care industry

TOUCH Scrushy is famously obsessed with the smallest details, though he does deny that he once ordered an exec to leave the room because his tie wasn't on straight

in its infancy, Scrushy thrived in the rough-and-tumble race for business. Six months after joining LifeMark, he vaulted to vice-president in charge of a \$100 million division. When he was still in his twenties, Scrushy marched into the office of LifeMark Chief Operating Officer Paul Frison and declared, "I at least want your job and someday intend to become chairman," Frison recalls.

Scrushy did better than that: He built a healthcare empire. After LifeMark was acquired, Scrushy and four others in 1984 started HealthSouth, each chipping in for a total of \$50,000. The team, later joined by Larry House as chief operating officer, created a behemoth out of the bits and pieces of a fragmented industry, gobbling up diagnostic, surgery, and rehab centers in 50 states.

To drum up PR, Scrushy sang and played piano in a country and western band that performed at health-care conventions. The band was good enough

that people attending the conventions even asked for Scrushy's autograph, he recalls. He later pursued contracts with professional sports teams and staged glitzy shows with such superstars as Bo Jackson and Michael Jordan to talk to kids about health issues. He took the company public in 1986 and has since built it into a \$3 billion powerhouse. With net earnings up 34%, to \$342 million in 1997, the company is thriving.

Can Scrushy fix MedPartners? "We'll have to wait and see," says McGowan, who controls 5 million shares. Others have more faith. "He's one of the few people in health care who have successfully made the transition from entrepreneur to running a multibillion-dollar company," says James Hoover, a partner at New York venture-capital firm Welsh, Carson, Anderson & Stowe. Of course, that's what they used to say about Rick Scott and Steve Wiggins.

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BULLS AND BEARS,
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BEEN A WOLF.

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NEVER CROSS A BOND DEALER

Larry Fondren tried to demystify the market. Bad move

To many observers, the bond market operates much like a souk. There is no formal exchange, no central posting of bids and offers, no registry of trades once they occur. Hundreds of bond dealers trade more than \$400 billion worth of securities a day over the telephone and by fax machine, and they thrive on the lack of public information. Investors, who have no way of knowing if dealers are quoting prices that have been marked up steeply, are at a disadvantage.

So when Berwyn (Pa.) entrepreneur Larry E. Fondren offered an electronic service that took some of the mystery out of the bond market and cut trading costs, he thought it would be a roaring success. Some players, though, didn't think it was such a good idea. Now, Fondren is out \$10 million. His story could trigger closer inspection—and possibly major reforms—of the largely opaque bond market by Congress and regulators.

BASIC INFO. Fondren began small in 1985. He started the Exchange, a computer matching service for insurance companies looking to dispose of junk bonds that regulators wanted sold from their investment portfolios. The limited foray into the bond market convinced Fondren that there was a need for an electronic service that carried basic pricing information, similar to Instinet, the equity trading system of Reuters Holdings PLC. What information did exist

was anecdotal, and it came from a small number of mostly New York-based bond dealers, such as Bear Stearns, C.S. First Boston, Cowen & Co., and Merrill Lynch, rather than from a national market system such as the New York Stock Exchange or NASDAQ. Today, there are more than a dozen online services for the bond market, but all have limitations.

THE BOND BIZ

The U.S. bond market is huge. New issues totaled \$9 trillion last year, while total securities outstanding exceeded \$12 trillion. And daily trading volume totals at least \$400 billion a day. The most active areas are:

	BILLION/DAY
U.S. TREASURIES*	\$212
MORTGAGE-BACKED SECURITIES*	\$47
FEDERAL AGENCY DEBT (FANNIE MAE, FREDDIE MAC)	\$40
CORPORATE DEBT	\$10
MUNICIPAL SECURITIES	\$3

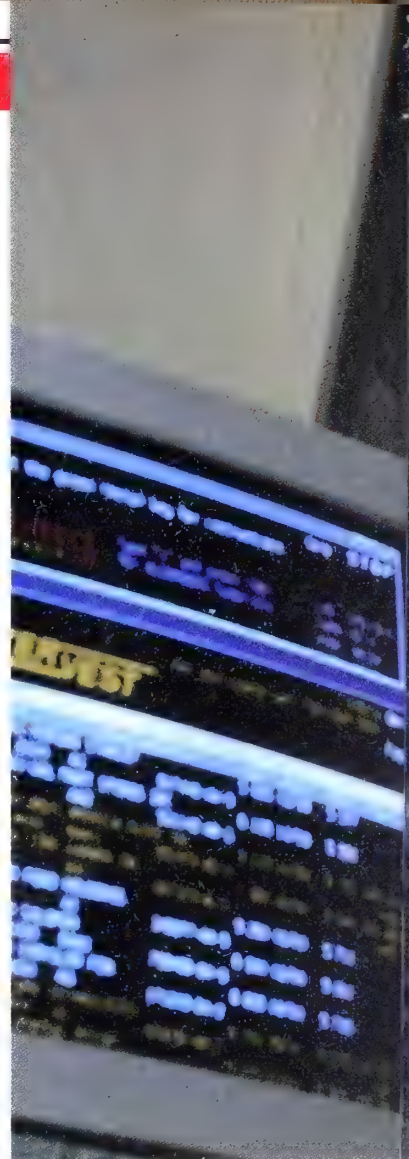
*Primary dealer activity only

DATA: BOND MARKET ASSN

transactions between institutions. The system, in theory, should reduce the cost of trading bonds by making the market more efficient. The average commission for an InterVest trade was 36¢ per \$1,000 transaction, split between buyer and seller, according to Fondren. By comparison, the average markup on a corporate bond trade from 1995 to 1997 was \$1.875. During that period, corporate bond buyers were

After several years of research and trials, Fondren in 1993 persuaded a small number of investors to back a radical new product: InterVest Financial Services, an electronic system for the estimated \$100 billion-a-day secondary market, in which bonds that are held in investor portfolios or in professional dealers' inventories are traded. And that's when his troubles began.

With Securities & Exchange Commission approval, he offered what no other service had: electronic posting of bids and offers, the ability to make trades at the push of a button, and anonymous



BAD BREAK: Fondren has lost millions and may soon be out of business

overcharged \$41 billion, says Fondren. Fondren then asked Bloomberg Financial Markets, which carries other third-party services, to carry his system. Bloomberg agreed, but six months before InterVest's scheduled debut in 1996 it backed out. While Bloomberg eventually relented, Fondren believes it did so only after the Justice Dept. and the SEC began an informal investigation into whether dealers were colluding to keep InterVest from growing. Bloomberg refuses to comment on the episode.

FEW TAKERS. In December, 1996, InterVest began appearing on Bloomberg. But it never really caught on. Problem was, InterVest made dealers unhappy. It reduced the need for their services as middlemen between buyers and sellers. Indeed, only a handful of bond dealers

Wall Street "didn't like what InterVest was about," says



THE INTERVEST SAGA

1985 Entrepreneur Larry E. Fondren starts the Exchange, a computerized insurance-policy database.

1992 Fondren receives SEC approval to become an electronic junk-bond broker. He later wins SEC approval to expand service to municipal bonds and government securities.

MARCH, 1993 InterVest begins trading.

AUGUST, 1995 Bloomberg agrees to carry InterVest as part of its menu of services for fixed-income dealers and investors.

JANUARY, 1996 Bloomberg balks before product's debut. Fondren's complaints trigger informal Justice Dept. and SEC inquiries into whether dealers were trying to block InterVest from appearing on Bloomberg.

MARCH, 1996 Bloomberg relents, agrees to let InterVest begin trading. Later, Justice and SEC turn up no evidence of dealer collusion.

DECEMBER, 1996 InterVest appears on Bloomberg, but it never really catches on.

JANUARY, 1998 Fondren claims 130 subscribers, most of whom are institutional investors. InterVest still lacks dealer participation. In desperation, Fondren lets corporations issue bonds directly to institutional investors, thus cutting out dealers as middlemen.

FEBRUARY, 1998 Bloomberg abruptly cuts off InterVest without explanation.

DATA: BUSINESS WEEK

osted their prices on InterVest. Thomas A. Price, a senior vice-president at Bank of New York's Bond-an electronic trading service for clients: "The Wall Street community didn't like what InterVest was about, so they boycotted it. They put [Fondren] in the penalty box." Adds James W. Toffey, president and CEO of TradeWeb, a new Internet-based service formed for four investment banks: "Dealers are market makers and they work for their customers. That's the way the world works. Maybe [the bond markets] aren't ready to be mixed up." Fondren says some 130 firms used InterVest. But most were on the "sell" side of the market—institutions such as life insurers, money managers, pension funds that buy securities for their portfolios. Only a small number actually used InterVest to transact business with one another—about

25 orders per day on average—and the typical size of each trade was relatively small, about \$2 million. By the end of 1997, Fondren didn't have enough subscribers to keep the system going, and he had run out of money.

Thinking he had nothing to lose, Fondren in late January of this year advertised that InterVest was available for corporate bond issuers to sell directly to institutions. "It caused an uproar," says Fondren, "because dealers didn't like that I was cutting them out of new issues."

A week later, Bloomberg dropped InterVest. Fondren believes Bloomberg did so because of either real or perceived pressure from dealers, who are important Bloomberg customers and valuable sources of bond-market information. A Bloomberg spokeswoman denied this was why InterVest was cut off.

Dealers claim there was never a boy-

cott. They speculate that Bloomberg wasn't convinced InterVest would ever become a commercial success. If dealers don't like a service, it has no hope of getting the critical mass of transactions that make a market functional. InterVest failed because "nobody likes going to a party until there are lots of other people there," says Christopher J. Carroll, managing director of global electronic trading for DMG.

HIGH COSTS. Washington authorities are watching Fondren's experience. Lawmakers who oversee securities trading could begin an inquiry—somewhat like the 1993 congressional effort to create a reporting system for government bonds, which was beaten back by dealers. "We've long known that the bond market's a big mystery to most investors," says one GOP aide. "It would be in the public interest if we could make it more transparent."

SEC officials also would like the bond market to be more accessible and to offer more information on prices and trades. But the commission prefers to let the private sector do the job. While the SEC since 1975 has had the power to require corporate bond trades to be reported, for instance, the agency

has never used it.

University of Chicago finance professor Paul Schultz, one of the authors of a landmark 1994 study of the NASDAQ market that found widespread collusion among dealers, has been studying the bond market, and he doubts that he'll find NASDAQ-type collusion. A Justice source says so far they've not seen evidence of that sort of behavior. Still, Schultz expects his study will find that trading costs are "fairly high."

So what is Fondren's fate? He currently is trying to raise \$10 million to switch InterVest to an Internet-based bond service. Otherwise, InterVest will go out of business. "I mortgaged my house, my wife sold her jewelry, and even my employees have lent me their savings," says Fondren. He may have a better mousetrap, but so far the world isn't beating a path to his door.

By Paula Dwyer in Washington

executive. "They put [Fondren] in the penalty box"

PROSECUTIONS

HEAT FROM THE BOILER ROOM

Will Bear Stearns get burned by the A.R. Baron case?

Feb. 23 was John McAndris' birthday. For the former chief financial officer of A.R. Baron & Co., the defunct micro-cap brokerage, this was a birthday to remember—because it was also judgment day. On that rainy Monday afternoon, a New York State Supreme Court jury began considering 25 felony counts that could send the mild-mannered grandfather to prison for up to 25 years. But whatever the verdict, the trial has troublesome implications for the array of brokers, firms, and stock promoters mentioned in the six-week trial—notably Baron's clearing firm, Bear Stearns & Co. The trial shed new light on a nagging question: Was Bear Stearns aware of illegal activities at Baron?

The trial revealed close, even intimate, links between Bear Stearns and Baron. Among other things, testimony pointed to a close relationship between former Baron Chief Executive Andrew Bressman—

who has pleaded guilty to illegal activities at Baron—and Bear Stearns' chief of clearing, Richard Harriton. Bear Stearns' links to Baron are being scrutinized by Manhattan District Attorney Robert M. Morgenthau, and the trial indicated yet another "spin-off" investigation, mentioned in testimony by a Morgenthau investigator. The target of that inquiry is also unclear, though prosecution witnesses testified that they had been questioned about D.H. Blair, a 300-broker firm with customers around the country. A Blair spokeswoman said

CLOSE TIES

Was A.R. Baron's clearing firm, Bear Stearns, aware of illegal activities at the micro-cap firm? A trial reveals intimate links



testing the suits.) Bear Stearns has denied knowledge of illegal actions at A.R. Baron and has also pledged cooperation with all inquiries.

The Bear Stearns-Baron link emerged from the prosecution's effort to prove that McAndris knew about alleged illegal trading at Baron. Defense lawyer John J. Rieck Jr. maintained that Bear Stearns knew at least as much as McAndris, if not more. As part of the contention that McAndris was guilty of enterprise corruption—the state anti-racketeering law—prosecutors alleged that Baron traders, supervised by McAndris, engaged in rampant unauthorized trading to prop up share prices. Customers, claiming they never placed the orders, refused to pay for the trades when they received their confirmation slips from the clearing firm, Bear Stearns. And that allegedly resulted in an extremely high rate of "sellouts" forced sales of stocks when customers won't pay.

Prosecution witnesses testified that sellouts were so astronomical that McAndris had to have known that



were red flags for illicit trading. According to former Baron trader Charles Plaia, the rate of sellouts was as high as 60% to 70% of trades for months at a time. In a grueling cross-examination, Plaia, Rieck expressed wonderment that "Bear Stearns didn't come running into A.R. Baron" to ask the traders, "What the heck is going on?"

Or would they? According to the transcript of Feb. 10 court discussion aside the hearing of spectators, prosecutor Eric R. Nallo observed that Bear Stearns' "position is as long as they have their money in a certain place, they don't care if the place closes down as long as they are covered." For his part, Plaia testified that Bear Stearns was aware of the sellouts. He said that he and trader Nicholas Marino were both notified "why Bear Stearns kept us open and didn't 'know what kind of relationship Bressman and Bear Stearns had."

Similar views were brought out

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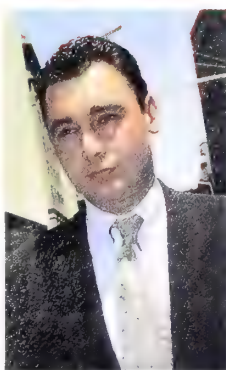


the cross-examination of another prosecution witness, Roman Okin. (Both Plaia and Okin were indicted along with McAndris, and pleaded guilty to one count of enterprise corruption, as did Bressman and Baron.) The former star broker, who earned millions at Baron and was a part-owner of the firm, said he and Bressman would discuss that "we had a lot of sellouts and a lot of liquidations, and at times it looked like" Baron was "parking" stock—putting stock in customer accounts for a short period to manipulate share prices. As a result, Okin testified, he felt that "if they're not stupid, Bear Stearns will catch on." Okin said he "had a suspicion Bear Stearns was aware we were breaking a lot of securities rules and conducting business in an illegal fashion."

Okin testified that Bressman and Bear Stearns clearing chief Harriton were in close contact. He alleged that the two met for lunch every week, and that Harriton was also a guest of Bressman's at a New Jersey country club. Under questioning by Rieck, Okin said he didn't know the specific reason for the lunches—which McAndris did not attend—but did have a "general idea" they discussed "our financial situation." Okin added that he was never told by Bressman that they discussed illegal activity, or that Harriton suspected illegal activity at Baron. But Okin testified that he and Bressman both suspected Harriton was aware of chicanery at Baron.

Neither Bressman nor Harriton shed light on the subject. Both were subpoenaed by Rieck, but neither was called to testify before the jury by either side. Bressman, testifying outside the presence of the jury, invoked his Fifth Amendment privilege and refused to answer any questions. A Bear Stearns spokesman, Larry Rand of Kekst & Co., said that Okin was wrong—that Harriton did not have weekly lunches with Bressman. Rand declined further on-the-record comment on the questions raised by the trial.

Some of the trial testimony pointed to Bear Stearns as a kind of stern overseer of Baron—demanding, for example, that Baron conduct its "sellouts" by selling to "the Street and not by shifting to other accounts within the firm. Indeed, Okin and Plaia both testified that a Bear Stearns official—one of two delegated to the task—occasionally monitored trading



WITNESS: *Former Baron star broker Okin pleaded guilty to a felony*

at the Baron trading desk. If the two Bear Stearns officials hung around enough, apparently they would have seen a lot. Plaia and Okin both testified that a stock promoter, Ray Irangy, frequented the Baron trading desk in 1995 and 1996, in violation of rules prohibiting outsiders from the trading floor. (Irangy was indicted for stock fraud by a federal grand jury in October, 1996, in a case unrelated to Baron, and subsequently pleaded guilty.) If Irangy was at the trading desk, it would be hard not to notice him—the trading room was just 15 feet by 30 feet. Moreover, testimony indicated that Irangy may have been at Baron at about the same time as the two officials—though there was no testimony that Irangy met either Bear Stearns representative.

In his testimony, Plaia said that Baron came under intense pressure from Bear Stearns to get shares off the

books—a perfectly legitimate response to what Bear Stearns perceived as excess market risk. Plaia said that when McAndris, because of the Bear Stearns pressure, ordered him to get the shares out of Baron's trading account, he acted by sending the shares "into space." By that, he meant illegally putting the stocks in customer accounts without their knowledge.

Plaia said that when shares were sent into "space," they were handled differently than ordinary, authorized buyers. Both types of trades would be immediately entered into the NASD system. But ordinary trades would be immediately entered into the Bear Stearns system as well. Plaia testified that phony trades would all be entered into the Bear Stearns system at the end of the day. The firm would then generate confirmations for the customers—and they would often refuse to pay. If there was an after-close avalanche of buy orders, could that have been a tipoff to Bear Stearns that possibly illicit trading was taking place? That is one of the most intriguing questions raised by the Baron trial.

Other firms and persons also found themselves snared by the wide-ranging testimony. Okin testified that he paid a Merrill Lynch & Co. broker \$3,000 to \$4,000 in cash in return for selling Baron stocks to his customers. A Merrill spokesman said the broker no longer works for the firm, and that Merrill had no knowledge of any payoffs to the broker. Other testimony from Okin pointed to alleged improper trading at D. H. Blair, where he worked before coming to Baron. The testimony also featured a host of minor characters, such as a stock promoter who Plaia maintained gave him \$120,000 in a brown paper bag that weighed a little more than a "medium-size ham." Plaia testified that he drove from the stock promoter's Long Island home into New York, gave the money to Bressman, and "we thanked each other."

McAndris was not implicated even indirectly in receiving cash payments. But prosecutors maintained that he knew what was going on. Some of the most damaging evidence consisted of a sworn statement from McAndris to prosecutors contend, put forth a false picture of Baron's financial position. The stuff—but if the prosecution prevails that could be enough to send McAndris to prison for a long time. Conviction or acquittal, however, may prove to be mostly a side issue—if other shoes begin to drop.

By Gary Weiss in New York

WHO'S WHO IN THE BARON TRIAL

ANDREW BRESSMAN

Former chief executive of A.R. Baron, he pleaded guilty and pledged cooperation—but against whom? He was not called to testify by the prosecution.

RICHARD HARRITON

Bear Stearns' head of clearing. Okin testified that Harriton lunched weekly with Bressman and was a guest of his at a New Jersey country club.

JOHN McANDRIS

Former chief financial officer, accused of being a member of the "inner circle" that ran A.R. Baron—which he vigorously denies.

ROMAN OKIN

Ace Baron broker and the prosecution's star witness. Testified about ripping off clients for millions of dollars.

CHARLES PLAIA

A trader at Baron, he testified about seeing such illegal acts as "sending stocks into space"—phony trades—as well as bribes.

DATA-BUSINESS WEEK

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HOW MANY BANKERS CAN YOU SQUEEZE INTO SAO PAULO?

With fees tight, a slew of foreigners vie for Latin business



Investment bankers making the 11-hour journey from New York to São Paulo used to be able to get some work done on the plane. Not anymore. "The flights are filled with your competition," says Alberto J. Verme, managing director at Salomon Smith Barney. They've all piled into Latin America chasing what they hoped would be a rich lode of new business.

Trouble is, there are too many investment bankers chasing too few Latin deals. Asia's financial crisis and a subsequent slowdown in Latin economic growth is cooling demand for new equity offerings. At the same time, everyone from Wall Street's Merrill Lynch & Co. to Spain's Santander Investment is fighting hard for market share (table).

With trading commissions and advisory fees falling fast, the banks that survive will be the most flexible ones—those able to diversify from equities to debt to corporate finance. "Every time you have a hiccup in the region, you have to shift resources across product areas," says Tim Purcell, co-head of Latin American mergers and acquisitions at J.P. Morgan & Co.

For now, the big money is being made in debt underwriting and trading. In 1997, 75% of the total of \$750 million in Latin investment banking fees came from such activities. Foreign lenders also are moving into high-growth ar-

reas—asset management, for instance.

Failure to adapt to the changing investment climate is what forced ING Barings Ltd. to retreat from Latin America. The investment bank dumped its Latin equities business and fired 150 in February even though it produced solid research and traded an estimated 10% of the region's American depositary receipts. The bank insists the operation was profitable. Yet some competitors contend that ING Barings' business became publishing its research—not moneymaking.

Still, other banks are in the region for the long haul. They're attracted by the promise of long-term economic growth,

THE SURVIVORS

MERRILL LYNCH

Strong local presence

J.P. MORGAN

Tops in mergers and acquisitions

MORGAN STANLEY DEAN WITTER

Leading key Brazilian privatizations

SALOMON SMITH BARNEY

Building diversified businesses via local partners

SANTANDER INVESTMENT

Top foreign trader through investments in banks across the region

\$30 billion in Brazilian privatization this year, and fast-developing capital markets. The big winners are likely to be the U.S. firms. With three-quarters of all foreign investment in the region coming from the U.S., Latin companies are looking for banks with North American distribution.

The Wall Streeters are also moving aggressively to capture key privatization deals and advise on M&A. Total Latin American M&A activity nearly doubled from \$36.5 billion in 1996 to \$70.5 billion last year. J.P. Morgan led the region's M&A activity with a total deal volume of \$12.8 billion. But the real action is in Brazil, which accounted for 35% of Latin M&A deals in 1997. In February, Morgan Stanley, Dean Witter, Discovery & Co and Salomon Smith Barney were the bidders to advise the government on selling Brazil's \$40 billion phone company, Telebrás, by charging a commission of just 0.07%. The fees on Telebrás, which will begin privatization this year, are more than a full percentage point less than those on last year's \$3 billion privatization of Brazil's mining giant, Companhia Vale do Rio Doce. **"LESS THAN IDEAL."** Competitors are griping, but Corrado Varoli, a managing director at Morgan Stanley, says Latin team is looking toward the future. Investment banks, he says, "are not profitable in the U.S. that they can accept less than ideal profits in Brazil now, in hopes that in 10 years we'll have a more developed market."

Such talk isn't daunting several European banks, despite the ING Barings retreat. Take Spain's Banco Santander, which has invested \$3.5 billion in banks in eight Latin countries, built up a strong local equity research network, and is leading foreigners in equity trading volume in the key markets of Brazil and Argentina. With a Wall Street unit trading Latin American Depository Receipts, Santander Investment's research operation is "paid for, and then some," says Managing Director Jaime de Pineda.

Others are expanding through acquisitions. Salomon Smith Barney has lined up local partners in Brazil, Argentina and Chile, while SBC Warburg Direct Read is buying Brazil's Banco Omega Group. And Goldman, Sachs & Co. is negotiating to acquire a stake in Accio, the brokerage arm of Mexico's leading financial group, Banamex-Accival. No foreign lenders must make those investments pay off. Their bankers are hustling up new deals, or some of them may end up on the next flight home.

By Elisabeth Malkin in Mexico and Kerry Capell in New York, Ian Katz in São Paulo

...to Milan for a last-minute meeting.

...and took ten clients to dinner instead of just one.

...did more

...when you had to head for Hong Kong before



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...to preserve your time.

...ing. (And anything is usually what happens.)

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Cards

BY GENE G. MARCIAL

CLAIRE'S COULD SPARKLE AGAIN

Money manager Scott Black is a dedicated value player who would not think of buying junk. But he's accumulating shares of what he calls a "junk jeweler": Claire's Store (CLE), the leading retailer of low-priced accessories, mainly for teenage girls. "This company is no junk, though," insists the president of Delphi Management in Boston, which manages more than \$900 million. Claire's earnings have jumped at least 15% in each of the past five years.

Even so, the stock has drooped—from 24 two months ago to 15 on Feb. 9. Since then, it has edged up to 17. As others bailed out, Black seized the chance to buy. He notes that such picks have helped Delphi reach a compounded annual return of 21.3% for five years vs. 20.2% for the Standard & Poor's 500-stock index. In 1997, Delphi gained 40.2%, vs. the S&P's 33.3%.

What was behind Claire's dive?

LOOKING LIKE A 'JUNK JEWELER'



DATA BY COMENET FINANCIAL MARKETS

A certain amount of panic selling hit the stock when Les Dunavant, president of the Claire's Boutiques unit, suddenly resigned at the close of trading on Jan. 26. But earlier that day, before the company announced his departure, shares fell 18%, to 16. Investors were concerned that the turnaround Dunavant had spearheaded at Claire's Boutiques, catering to very young customers, could be in jeopardy. Executive Vice-President Mark Hoffman has assumed Dunavant's post. His leaving "didn't have anything to do with health," says Glenn Canary, Claire's investor-relations officer, but he wouldn't comment further. But Black is far from worried: Chairman and CEO Rowland Schaefer "has always been in charge, and he will continue to do a superb job running the company," says Black. For the year ended Jan. 31, 1998, Claire's reported a 29% jump in basic

earnings, to \$58 million, or \$1.21 a share, on sales of \$500 million.

The company, says Black, will surprise the Street with another record next fiscal year, when he expects earnings of \$1.44 on sales of \$580 million. He's impressed with the stock's 26% return on equity and the company's clean balance sheet: no debt and a cash hoard of \$2.80 a share. He sees Claire's climbing back to 24 in 12 months.

BANK PLUS LOOKS RIPE FOR A RAID

As California's thrifts consolidate, many of them are carving out niche markets to help them compete with superregional banks—such as First Nationwide, which recently agreed to merge with Golden State Bancorp.

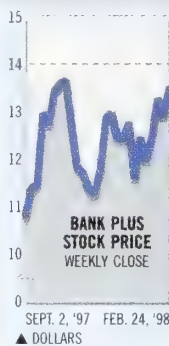
Nevertheless, "a number of the smaller California banks won't make it on their own," says Deborah Beylus of J.W. Charles Financial Services.

She says one savings and loan likely to be gobbled up is Bank Plus (BPLS) in Los Angeles, the holding company for Fidelity Federal Bank, which has 50 branches in Southern California and total assets of \$4.2 billion. "Bank Plus continues to be plagued with high operating expenses (72% of revenues vs. an industry average of 60%) and low net interest margins," notes Beylus. She thinks Bank Plus may not stay independent for long.

Despite the bank's troubles, speculation about a buyout has been heating up the stock. The price rose from 11 in early December to 14 on Feb. 3. In January, Tontine Partners, a New York investor group, upped its Bank Plus stake from 8.7% to nearly 10%, paying between 11 and 13 a share. Jeff Gendell, a principal at Tontine, declined to comment. Beylus, who expects Bank Plus to earn \$1 a share this year, compared with last year's 67¢, thinks the stock is worth 18 to 20 in a buyout.

Credit quality has been improving, notes Beylus, with the bank's nonperforming assets and delinquent loans

RUMORS MAY BE UPPIING THE PRICE



DATA: BLOOMBERG FINANCIAL MARKETS

dropping to their lowest levels since December, 1991. Even so, the ratio of problem assets to total assets is higher than industry norms. But, she adds some of its consumer services would be attractive to large banks seeking a niche market: Bank Plus, for example, acts as a cash-services provider for a national network of automated teller machines operated by Americash. In addition, Bank Plus has just taken the first steps toward Internet banking.

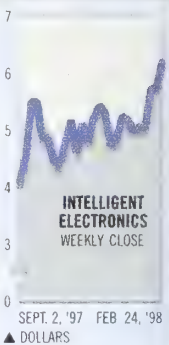
AN INTELLIGENT ELECTRONICS BUY?

Shares of Intelligent Electronic (INEL) are in the limelight, after languishing in the 4-to-5 range. The stock has climbed above 6 on relatively heavy volume—with no new to account for it. What's fueling the rise?

The company, through its 80% owned XLconnect Solutions (XLCT), provides information and technology to network integrators and resellers. An XLconnect, which trades at 16 a share, has caught the eye of several electronic biggies, according to some analysts. Whispers are that one of them will try to acquire Intelligent Electronics, with a market capitalization of \$258 million, to get their hands on XLconnect, which has a market cap of \$266 million. A spokesman for XLconnect declined comment. Right now, each share of Intelligent Electronics contains \$5 worth of XLconnect. James Meyer of Janney Montgomery Scott, a Philadelphia investment firm, figures XLconnect on its own is worth 20 to 25 a share and Intelligent Electronics about 10.

He notes that, apart from its 80% stake in XLconnect, Intelligent Electronics has some \$70 million in cash plus some tax-loss carryforward. The company also has four computer stores, with annual sales of about \$20 million. XLconnect, for its part, posted revenues of \$135 million last year and earnings of 30¢ a share. Analysts expect earnings of 55¢ in 1998.

THE LIGHT HAS BLINKED ON



DATA: BLOOMBERG FINANCIAL MARKETS



INTERNET

DOWNLOADING THEIR DREAM CARS

buyers are using the Internet to snag great deals

When Rhona Pearl wanted to buy a new car in December, she did what a growing number of savvy shoppers are doing: she turned to the Internet. Looking to bargain up from the dealers' sticker price, Pearl, a Manhattan marketing specialist for a car company in Agoura Hills, Calif., used the World Wide Web to find out dealers' wholesale costs. Then she asked for bids from online car-buying services Microsoft CarPoint and Auto-By-Tel. Their dealers got back to her the following day, and Pearl drove home with the car of her dreams, a sporty black 1998 Honda Prelude that was \$500 above the invoice price. "It was very, very simple, a pleasurable experience," she says. "It took all the game-playing out of buying a car." Whether it's to look up information, get a dealer referral, or actually make a purchase, more consumers are using the Internet to take the shock out of sticker

prices. Market researcher J.D. Power & Associates Inc. says 16% of new-car buyers used the Web for shopping last year, up from 10% the year before, and 4% went so far as to try out an online buying service. Industry experts figure that 2% of the 15 million new cars sold last year were a direct result of purchase requests funneled to dealers by such services as Auto-By-Tel, Autoweb.com, and CarPoint. That's roughly \$6 billion in business.

And that's just a smidge compared to what's ahead. A January survey by dealer consultant Dohring Co. in Glendale, Calif., found that 10% of consumers said they would be willing to buy a car online, and without a test drive, up from 4% a year earlier. "Realistically, we think

PEARL, IN NEW PRELUDE: "It took all the game-playing out of buying a car"

two years from now half of all new-car buyers will use the Internet in the shopping process," says Thomas G. Libby, a director at J.D. Power in Agoura Hills, Calif.

That could have a profound impact on car dealerships and auto makers. Armed with information from the Web, buyers are already beginning to exercise more bargaining power than ever before. That's bound to force selling prices down, slicing into the dealers' already thin margins. New cars, for example, gross dealers an average of \$1,440, or 6.4%. With cybershoppers saving a couple hundred bucks each purchase, that could shave the margin by nearly a point. The result: Further consolidation among dealers that don't have enough volume to weather lower margins.

Secretly, carmakers couldn't be happier. With distribution costs making up nearly a third of a car's costs, many auto makers have been trying for years to reduce the number of dealers to make the system more cost-effective. Four or five large dealerships in a metropolitan area could cover the territory at a lower cost and higher profit than a dozen or more do now. "The Internet is helping accelerate the trend toward consolidation," says Matthew J. Ericksen, vice-president of Boston Consulting Group's Chicago office.

CUSTOMER CONTROL. It's also helping carmakers get Net-savvy. Today, Chrysler Corp. and General Motors Corp. are taking a Web page from online upstarts. Both are experimenting with their own Net sites that link online shoppers to dealers in a handful of regions. Now Chrysler is hatching a plan to go nationwide. "For the first time, the customer is going to control the retail system," Chrysler Chairman Robert J. Eaton told dealers at the National Automobile Dealers Assn. meeting in late January.

Chrysler's Web site has a "Get a Quote" feature that allows buyers in Maryland and California to specify the car they want, search out a dealer, and get a price. That's led to 600 car sales in its first six months. GM offers something similar in the West. More than 400 of its 700 dealers in four Western states have gone online with GM's BuyPower site, which lets shoppers search dealers' in-

"For the first time," says Chrysler chief Eaton, the customer will "control the retail system"

Information Technology

ventories for cars. GM BuyPower has had 240,000 visitors since its September launch. The company is considering taking the system national.

Other carmakers, including Ford and the Japanese outfits, are less aggressive with their Web sites. They offer little more than electronic brochures with prices, specs, and local dealers. "For most manufacturers, the Internet is still something of a blind spot," says Jeremy P. Anwyl, a Santa Ana, Calif., auto-retailing consultant.

Indeed, the carmakers are in a bind. As much as they'd like to use the Net

her newfound ammunition to a local Honda salesman. "I came in with everything on a spreadsheet. It kinda blew him away," she says. "He kept leaving to 'check with his manager,' but every offer he came back with had some kind of spin on it." So Pearl went back to her computer and submitted purchase requests to CarPoint and Auto-By-Tel.

Those services sign up dealers who pay a fee to receive online referrals. Auto-By-Tel, for example, charges dealers from \$500 to \$2,500 per month, depending on the brand or franchise, location, and territory size. In return, they

able to find the car cheaper in a local dealer's showroom.

The services are beginning to crumble. "Some dealers bought in to secure the territory, but then they don't service it," says Peter R. Ellis, a former car dealer who founded Auto-By-Tel Corp. in Irvine, Calif. Auto-By-Tel replaced 150 of its 2,700 locations last year, he says, "and we'll drop 400-500 more over the next couple of years."

For dealers who get it, the system works. Don-A-Vee Auto Group in Pomona, Calif., the state's largest Jeep dealer, now does nearly 25% of its ne-

EVERYTHING EXCEPT A WAY TO KICK THE TIRES

AUTO-BY-TEL

WWW.AUTOBYTEL.COM

Service started 1995
2,700 dealers

Biggest buying site offers new and used cars through dealers who pay up to \$2,500/mo. for exclusive referrals. Financing, leasing, and insurance available. Site accepts no advertising. 1997 revenues about \$16 million; responsible for about \$500 million in monthly car sales.

AUTOWEB.COM

WWW.AUTOWEB.COM

Service started 1995
2,100 dealers

Sells new and used cars by referring requests to multiple dealers who pay \$25 for each. Financing, leasing and insurance available. Individuals can list used cars for \$19.95/mo. Subscription fees from dealers made up most of \$4 million in 1997 revenues.

CHRYSLER GET A QUOTE

WWW.CHRYSLER.COM

Pilot started 1997
California, Maryland
dealers
National rollout planned

Buyers can choose a model, search out the nearest dealer who stocks the exact car, and request a price quote. Site lists equipment and dimensions of competing models, but not prices. Prices are list, not invoice.

GENERAL MOTORS BUYPOWER

WWW.GMBUYPOWER.COM

Pilot started 1997
California, Washington,
Oregon, Idaho dealers

Allows buyers to specify a model, search for it in a dealer's inventory, get a quote, arrange credit, and schedule a test drive. Site has independent comparisons to competing models. Prices given are suggested list, not invoice.

MICROSOFT CARPOINT

WWW.CARPOINT.MSN.COM

Service started 1997
1,095 dealers

Refers buyers to new- and used-car dealers, who pay a monthly fee up to \$1,600. No financing or insurance. Used-car database from marketing partner Reynolds & Reynolds. 1997 revenues estimated less than \$2 million; started accepting ads in January.

to direct sales to high-volume dealers and get rid of the weaker ones, they don't want a dealer backlash caused by telling consumers where to get the best price. And, because of state franchise laws, carmakers find it difficult to deny dealers access to their sites. "They're looking for ways around the laws, like letting only dealers with the highest customer-service ratings get at their Internet customers," Ericksen says.

AMMUNITION. So how does it work? Typically, shoppers log on to the buying services or information sites like Edmunds and Kelley Blue Books to learn the invoice price of a car, options, and to figure out how much their trade-in is worth. Some stop there. "It looks like 60% to 70% of people coming to our site never want a referral," says Alex Simons, product manager for Microsoft Corp.'s CarPoint. "Basically, they're arming themselves for a trip to the dealer."

That's how Pearl started, by taking

get the right to all the referrals from a group of ZIP codes. Others, including CarPoint and Autoweb.com, aren't as exclusive. They'll sign up competing dealers and let the shopper pick from them. The dealers agree to contact the shopper by phone with a best-price deal.

Still, the electronic car-buying services are far from perfect. For one, there's no guarantee that the service will send the request to a dealer. Autoweb.com can't deliver fully half the requests it gets simply because it doesn't have a dealer close enough to the buyer, admits co-founder Payam Zamani.

Some dealers even welch on the deal. Ask Alison Ross, who runs a small business in Atherton, Calif. Ross put in a bid to Auto-By-Tel last summer, but after they didn't respond, she called them. They gave her the number of a dealer in her area, who didn't call her back. So Ross calculated the price from information on Auto-By-Tel's site. But she was

car business through the Web, up from less than 5% a year ago. It converted about 50% of its referrals into sales, well above the 18% to 20% closing rate that the buying services say is usual. "It didn't work until I set up a separate sales force to handle the Internet," Clive Skilton, the company's owner.

The difference: Inquiries now get an immediate E-mail response, and sales team works on salaries instead of commissions. Skilton can offer deep discounts to consumers because he pays no commissions, and Web referrals cost less than advertising, which can run as much as \$450 per car.

For those that have computers, good news. They'll get the best price and without having to fight with a salesman until they're red in the face. For the others—well, all you have to do is outmaneuver that guy in the goof.

Larry Armstrong in Los Angeles
with Kathleen Kerwin in Detroit

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Developments to Watch

EDITED BY NEIL GROSS

MAYBE DOG TAGS WILL KEEP CHIPS FROM STRAYING

WATCH OUT, CHIP THIEVES. Pawning off stolen semiconductors is about to get a lot harder. The Electronic Industries Assn. has just adopted a new technology called Data Matrix that engraves an indelible microscopic code onto the outside of chips. This should make it far easier for law enforcement agents to track and recover stolen semiconductors.

Data Matrix was developed by CiMatrix in Canton, Mass.—a division of Robotic Vision Systems Inc. of Hauppauge, N.Y. The device works like a tiny bar code, but it contains 100 times as much information. That lets manufacturers mark each chip not only with a vendor ID and part number but also with individual serial numbers. Thieves can't remove the code without ripping off the chips' casings, which in most cases would destroy

the devices. Criminals will also have a tougher time passing off counterfeit parts, because any manufacturer of a product that incorporates chips can check the chips' pedigree.

That's music to the ears of the FBI and of underwriters such as Chubb Cos., which have watched with alarm in recent years as chip theft has ballooned into a multibillion-dollar racket. Lately, insurers have been paying out huge sums to cover stolen parts. Chubb, in particular, has been a major proponent of serialization—at one point sponsoring a project on technology-theft prevention.

The new codes won't wipe out the black market for stolen chips, says Bill Baker, CiMatrix' senior vice-president for worldwide sales. Some unscrupulous buyers will always accept cheap parts, regardless of their provenance. But the codes will give legitimate makers of PCs and other products a way to make sure that their chips are legit. *Andy Reinhardt*

HERE, KITTY: HAVE A CONTRACEPTIVE

IF YOU'VE EVER NOTICED the hundreds of cats prowling the Roman Coliseum—or the feline yowling in the backyard—you know there's a stray cat problem. An estimated 30 million to 60 million of them are roaming the U.S. alone. To reduce this population, Virginia-Maryland College of Veterinary Medicine in Blacksburg, Va., is developing an easily administered oral contraceptive.

Researchers extract pro-

teins from the outer membrane of feline ova and attaches them to salmonella bacteria that are rendered harmless. When ingested by female cats, the proteins trip an immune response. Antibodies attack the proteins and surround the cats' own eggs, blocking sperm from entering.

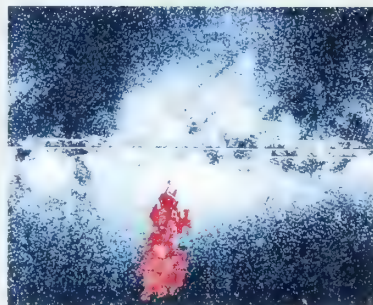
Dr. Stephen Boyle, a veterinary professor at the school, says the method could be commercialized within five years.

Catherine Arnst



A GALAXY SAYS: 'HELL, NO, I WON'T GO'

SOME ASTRONOMERS BELIEVE LARGE GALAXIES GROW by swallowing smaller ones. The Milky Way is no exception, says Johns Hopkins University astrophysicist Rosemary Wyse. For several billion years, it has been trying to absorb a dwarf galaxy called Sagittarius, pictured in red in this computer-enhanced photomontage. But Sagittarius is resisting, says Wyse. Less than one-hundredth



TOUGH DWARF: The Milky Way can't digest Sagittarius (in red)

the size of the large system, it likely has orbited the central regions of the Milky Way a total of 10 or 12 times, plunging deep into our galaxy as it goes.

Along the way, it should have been tugged to pieces by the larger system's gravitational pull.

How has Sagittarius escaped this fate?

Wyse believes there is more to the dwarf than meets the eye. "It's got a lot of dark matter, so it is able to hold on to its stars," she says. Scientists can't see or characterize "dark matter." But they suspect that it may account for as much as 90% of the total mass of the universe. □

SOON, YOU TOO CAN EXTERMINATE PHONE BUGS

TECHNOLOGY FOR THWARTING wiretaps over the public phone network has been around since the 1950s. But high costs have confined its use mainly to intelligence and law-enforcement agencies. Now, Israel's Micro Link Ltd. is preparing to bring anti-wiretap technology to the commercial marketplace.

Founded by former army intelligence experts, the company has developed low-priced signal-processing chips that scramble phone calls using well-known mathematical encryption formulas, or algorithms. The chips will be encased in 4-inch, cube-shaped "black boxes," which must be attached individually to each secured telephone line.

Micro Link doesn't intend to market directly to individual or corporate customers. Instead, it hopes to sell black boxes to telephone companies, which would be responsible for installing them at customers' premises. The phone companies would likely charge about \$20 a month for the service. And, if required by local police, they would also maintain records of encrypted calls and cooperate with authorities in decrypting conversations.

Tsion Gonen, vice-president for marketing and sales at Micro Link, figures the company will be able to charge phone companies about \$250 per customer for the phone line. Israel's main carrier, Bezeq Telecom, has signed an agreement to use the technology. Micro Link also is negotiating with carriers in the U.S., Europe and Japan. *Neal Samuels*

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BusinessWeek **ONLINE**



ENTREPRENEURS

MILLIONAIRE DONS

Entrepreneurial vigor is flourishing in British academe

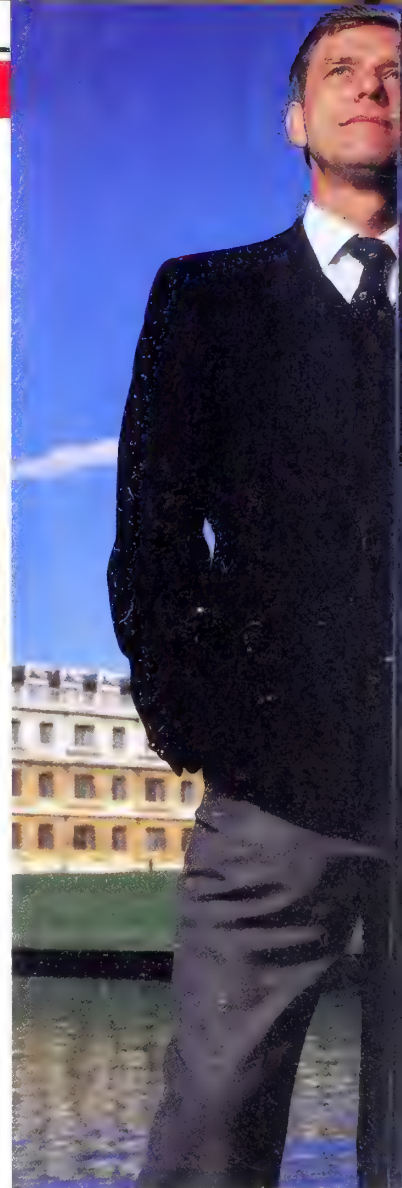
A hush descends over the timbered dining hall of Corpus Christi, one of Cambridge University's 31 colleges. The master, wearing a long black gown, says a prayer in Latin to end the evening meal. Afterward, the dons and dignitaries retreat to a private, wood-paneled room lit by silver candelabra. As port, elderflower cordials, and cigars are passed around, the conversation swings from medieval manuscripts to a less scholarly subject. David J. Greaves, a tenured lecturer, leans across the table and confesses he made a mistake with his first business venture, in high-speed phone and data networks. "Next time, I'll demand equity," says the 35-year-old computer scientist.

Cambridge's dreaming spires stud the sky just as they have for centuries. The teachers—called dons, from the Latin *dominus*, or master—still dine at high table and wear scholars' robes. But the buildings bustle with energy from something the old masters would have frowned on: entrepreneurship. Capitaliz-

ing on their intellects, Cambridge dons are patenting their discoveries as never before, spinning off startups and moonlighting with the likes of Hitachi, Xerox, and Microsoft. Although they're loath to discuss it, many are also starting to make great pots of money (table, page 101).

These technologically skilled men and women belong to Britain's growing tribe of "millionaire dons." Academics-turned-entrepreneurs, they feel as great an affinity for Intel Corp.'s Andrew S. Grove as for the groves of academe. Cambridge has spawned the most startups. But the same vigor, ambition, and iconoclasm can be felt in Leeds, Oxford, and Edinburgh. All told, Britain boasts at least 120 millionaire dons, says financial journalist Philip Beresford, who compiles an annual Rich List for the *London Sunday Times*. That's up from just a few dozen in the early '90s, he figures.

Britain clearly benefits from their growing presence. By providing the spark for technology transfer from universities to industry, these academics



represent a new means of generating wealth for Britain. With so much talent flowing between the ivory tower and high-tech startups, it's only a matter of time before universities produce a homegrown Intel or Microsoft Corp., says Christopher T. Evans, one of Britain's richest dons. Scientific entrepreneurship, he adds, is an "unstoppable beast."

NEW TOLERANCE. Both economic and cultural factors are spurring the dons to go into business. University salaries are low in Britain, especially compared to those in the U.S., so dons almost always look for ways to supplement their livelihoods. Full professors at the University of Cambridge make only \$67,000 a year. In addition, the universities seldom hand over patent rights to the scholars rather than guarding them closely as many U.S. institutions do.

Even more important, a younger generation of academics is moving away from bringing a tolerance for materialism. Fast cars, yachts, and estates—the trappings of success in Silicon Valley—



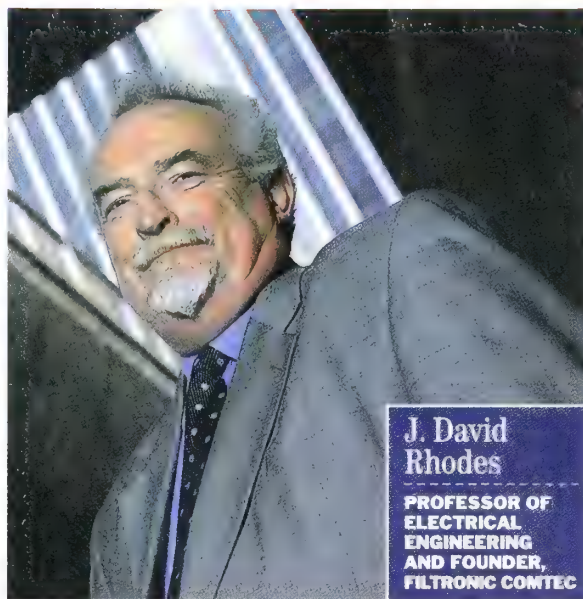
Hermann Hauser

CAVENDISH LAB
LECTURER; CO-
FOUNDER, ACORN
COMPUTER; VEN-
TURE CAPITALIST

t incentives for turning ideas into
acts. "I didn't want to be an acad-
dreamer," explains Evans, 40, who
started 15 companies and has a net
worth of \$115 million. "I wanted to
see things happen."

Who are Britain's millionaire dons?
They come from all walks of science and
engineering. Like their American coun-
terparts, most amass fortunes by licens-
ing their discoveries to established play-
ers or by starting venture-backed
businesses and taking them public.
Hauser, for example, got bitten by the
entrepreneurial bug while still a PhD
student at Hull University. He sold a
dozen leather-bound copies of his
thesis on bioengineered cocoa butter to
Cadbury Schweppes PLC—the company
that sponsored his PhD—for around \$125

thousand. With the proceeds, he bought a
house in the U.S., where he worked for
a tech startup. Returning to Britain,
he founded several biotech companies,
including Celsis International PLC and
Molecular Sciences PLC, both in Cambridge.



J. David Rhodes

PROFESSOR OF
ELECTRICAL
ENGINEERING
AND FOUNDER,
FILTRONIC COMTEC

Then there's high-profile millionaire
David E. Potter, a former physics lec-
turer at Imperial College who quit in
1980 to start a company in the booming
microcomputer market. Psion PLC now
has a market cap of \$554 million and is
a leading manufacturer of handheld com-
puters. No less successful is J. David
Rhodes. A 54-year-old professor of elec-
trical engineering at Leeds University,
he has founded four companies, includ-
ing Filtronic Comtec PLC. A mobile-com-
munications venture, Filtronic employs
1,000 people near Leeds and is capital-
ized at about \$336 million.

With their aura of achievement, these
powerful businessmen have inspired a
generation of young scientists. Like the
wealthier barons of Silicon Valley, many
millionaire dons invest time proselytizing
and coming up with programs aimed at
building entrepreneurial momentum.

Leading the charge is Cambridge-
based entrepreneur extraordinaire Her-
mann M. Hauser, 49. Austrian by birth,
he arrived at Cambridge in 1973 and
earned a PhD in physics. In 1978, he
founded Acorn Computer Group PLC
and built it into Britain's most successful
PC maker. When Acorn went public in
1984, Hauser's 50% stake made him a
millionaire. Soon after, Acorn's market
cap shot up to more than \$100 million.

**Bill Gates says he went
to Cambridge because
Needham wouldn't
come to Redmond**

The company faltered
when competing systems
running Microsoft's MS-DOS
operating system swept
Europe. But now, Acorn
has another shot at suc-
cess with a contract to de-
sign network computers
for Microsoft rival Oracle
Corp. These stripped-
down machines don't re-
quire hard drives or fancy
software since they pull
the programs they need
from a corporate network
or the Internet. If this
market takes off, Acorn
will be well-positioned,
having licensed its tech-
nology to a new Hauser-
backed company called
Netproducts that already
has a network computer

selling for \$500 at Harrods Ltd. and
other stores.

Hauser was never a full-time profes-
sor. His only formal links to Cambridge
are as a fellow at Corpus Christi Col-
lege and an occasional lecturer at its
renowned Cavendish Laboratory. Still,
he is Cambridge's biggest booster. He
has helped finance two dozen startups,
many based on the ideas of Cambridge
dons. Combined, his companies boast a
market capitalization of \$750 million.

LUCKY BREAK. One of Hauser's high-
profile bets is Cambridge Display Tech-
nology Ltd., which was spawned by a
lucky experiment in 1989. Physicist
Richard H. Friend and his postdoctoral
student, Jeremy Burroughes, were run-
ning electricity through organic materi-
als when Burroughes noticed a strange
green glow. What they had discovered
were light-emitting polymers—a prom-
ising candidate to replace liquid-crystal
displays in handheld electronic devices.

Before publishing their findings in
the scientific journal *Nature* in 1990,
the scientists spent \$1,650 of their own
money to take out a patent. Today,
Cambridge Display Technology is at-
tracting well-known investors. Hauser is
one, but there's also Intel, former Apple
Computer President John Sculley, Pow-
er Computing President Steve Kahn,
and American technology maven Esther
Dyson. CDT has licensing agreements
with Philips Electronics and Hoechst
and a joint-development agreement with
Japan's Seiko-Epson.

If CDT makes it into the ranks of dis-
play giants, it will have the unique mil-
lieu of Cambridge—as well as serendip-
ity—to thank. This ancient market town,
where punters lazily ferry tourists along

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exchange**

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I n c r e a s e i n B u s i n e s s V a l u e

iver Cam, has yet to produce a class company such as Oracle or ett-Packard Co. Yet it resembles ord University in the way that minted PhDs and professors com- mesh with the high-tech startup unity. And though total business y is just a fraction of Silicon Val- Cambridge-grown technology is ng to generate impressive returns: rea now boasts an estimated 1,200 ology companies. Unemployment is .3%, while average weekly wages % higher than the national average. se ties to America's high-tech com- ies have enriched the Cambridge

Last summer, the area's collec- ainpower drew none other than soft Chairman William H. Gates ho announced plans to spend \$80 n there for Microsoft's first non- research lab. Gates committed \$16 n to back local startups, and the rsity got a \$20 million donation his foundation for a computer lab. **HATS.** According to Gates, Mi- t was lured to Cambridge by peo- ch as Roger M. Needham, the for- head of Cambridge's famous ater lab and an expert in computer ty systems. Needham also was of the first directors of Cambridge ntants Ltd., the granddaddy of the echnical consulting firms. Later t by Arthur D. Little Inc., Cam- e Consultants spun off at least two companies.

icrosoft came to Cambridge because am refused to move to Microsoft's uarters in rainy Redmond, Wash. th a nod from the university—es- ly Vice-Chancellor Alec Broers, helped broker the deal—Needham ears three hats. He's a computer- e professor, pro vice-chancellor, salaried Microsoft employee. As ing director of Microsoft Research mbridge, he recruits scientists to at the software giant's new lab. edham's dual roles as a top uni- y administrator and Microsoft r have raised eyebrows. Some feel es Microsoft an advantage over niversity's other industrial part- such as Xerox, Glaxo Wellcome, hi, SRI, and Toshiba. Others ques- f the Cambridge region can ever ve the critical mass of Silicon Val- e the Seattle (Wash.) area, where soft is based.

ll, optimists see dynamics that call nd Silicon Valley in its early days. repreneurs demonstrate loyalty to nstitutions that nurtured them, and eeling is mutual. One symbol of ynergy is Alan J. Munro, a Cam-

bridge biochemistry professor who quit in 1989 to co-found Cantab Pharmaceu- ticals PLC. Four years later, Cantab was one of the first biotech companies to go public on the LSE. With a current mar- ket capitalization of \$193 million, Cantab could join the big leagues if its promis- ing cancer and herpes drugs pan out.

Munro, 61, has since returned to the university as master of Cambridge's

Christ's College. In the quiet elegance of the master's lodge, surrounded by an- tiques and books, Munro acknowledges the risks of Cantab's early days. Still, he says, he'd "do it all again" if he were 10 years younger. For enterprising acade- mics such as Munro, the Ivory Tower is no longer enough—but in many of the best ways, it's home.

By Julia Flynn in Cambridge

How Profs Are Creating Companies—and Wealth

CAMBRIDGE

ANDY HOPPER, 45

Communications-engineering professor; director of Olivetti & Oracle Research Laboratory. Helped found six local tech companies. His stake in Acorn Computer Group netted him an estimated \$10 million.

STEWART LANG, 49

Researcher at Cambridge University's Computer Lab. Helped found and now owns software company Micro Focus. Through trusts, holds stock worth more than \$8 million.

ALAN MUNRO, 61

Master of Christ's College. Co-founder of and scientific adviser to Cantab Pharmaceuticals. His stake in Cantab, traded on the London Stock Exchange and NASDAQ, is worth \$1.23 million.

CHRISTOPHER EVANS, 40

Visiting professor of biotechnology at Exeter, Manchester, and Liverpool universities. A venture capitalist specializing in biotech companies, his estimated net worth is \$80 million to \$115 million.

OXFORD

BRIAN BELLHOUSE, 61

Professor of engineering. Helped found Powderject Pharmaceuticals to commercialize a technology that may replace needle injections. His stake is worth \$20.5 million.

ALAN AND SUSAN KINGSMAN, 47 & 46

Professors of biochemistry and molecular genetics. Founded Oxford

Biomedica U.K., a biotech company that went public in 1996. Their 17% stake is now worth \$3.2 million.

W. GRAHAM RICHARDS, 58

Professor of chemistry. Helped found Oxford Molecular Group, which develops software for the drug industry. His stake in the company, which went public in 1994, is worth \$1.65 million.

LONDON, EDINBURGH, AND OTHERS

DAVID POTTER, 54

Former lecturer in physics at Lon- don's Imperial College. Founder and chairman of handheld-computer maker Psion Group. His family's stake in the company is worth \$184 million.

PETER DENYER, 44

Electronics professor at Edinburgh University. Co-founder and managing director of VLSI Vision, which designs

semiconductors for image sensing. His stake in the company, which went pub- lic in 1995, is worth some \$1.7 million.

JOHN KAY, 49

Director of Oxford University's new management school. Co-founded London Economics, a consulting firm valued at some \$11.5 million. Its ideas on a "stakeholder economy" have strongly influenced the Labour Party.

DATA BUSINESS WEEK. PHILIP BERESFORD

EDITED BY AMY DUNKIN

MARKET TIMING: A PERILOUS PLOY

The idea of marrying mutual-fund investing with market timing has innate appeal. With a phone call—or a few keystrokes at a Web site—you switch your money into equities when the stock market's going to rise and take it out before stocks go down. Who, after all, wouldn't want to ride the bull and dodge the bear?

Trouble is, market timing hasn't worked very well during Wall Street's 15-year bull market—certainly not as well as the tried-and-true approach of buy and hold. Take a look at the long-term record of market-timing newsletters offering advice for mutual-fund investors and money managers who run timing portfolios. Most of them trail the market and even the average diversified equity fund. Worse yet, if you attempt market timing outside a tax-sheltered account such as an individual retirement account or a 401(k), you'll cede around a third of your profits to Uncle Sam. That's because timers trade hyperactively, and profits on positions held less than one year are subject to the same tax rate as on ordinary income. Some mutual funds allow cash to build up, but almost none are outright timers.

GUESSING GAME. It's no wonder, then, that timers are unloved on Wall Street. Once-hot newsletters such as *The Elliott Wave Theorist* and *The Professional Tape Reader* have flamed out as the bull has run on and on. "Sometimes people have shown an ability to outguess the market in the short run," says Derek Sasveld, a consultant at Ibbotson Associates, an in-

vestment research firm. "Then conditions change, and they can no longer replicate that behavior."

Perhaps timers are scorned by the Establishment because they're a reminder of the 1970s, when Wall Street was in a funk. "That was the golden age of market timing," says Steve Shellans, editor of the *MoniResearch Newsletter* (800 615-6664), which reports on market-tim-

ing money managers. "The market went up and down, but at the end of the decade, stock prices were no higher. The buy-and-hold crowd made no money, but timers did."

Two decades later, the timers seem hopelessly out of sync. We asked *The Hulbert Financial Digest* (703 683-5905), which tracks investment newsletters, to

measure market-timing advice tailored to mutual-fund investors. In all, publisher Mark Hulbert identified 25 newsletters with 32 portfolios, since some newsletters have more than one timing

model. (Highlights of Hulbert's survey appear below. An extended version is available at www.businessweek.com.)

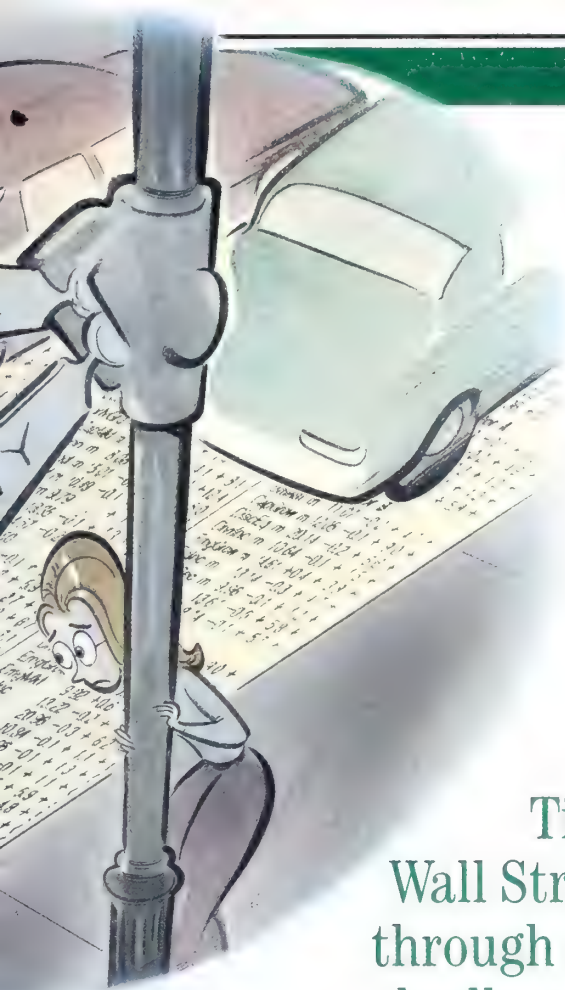


Few Medals for Market-Timers

NEWSLETTER	PORTFOLIO	10-YR. AVG. TOTAL ANNUAL RETURN*	ADJUSTED RETURN**
SYSTEMS & FORECASTS	"TimeTrend"	16.90%	18.81%
BOB BRINKER'S MARKETIMER	Aggressive Growth Fund Portfolio	15.81	17.23
MARKET LOGIC	Seasonality Timing System	15.73	23.51
THE BIG PICTURE	Master Key	14.99	17.52
TIMER DIGEST	"5 & 10" Consensus	14.92	15.73
FABIAN PREMIUM INVESTMENT RESOURCE	Domestic Fund Composite	13.41	14.46
PROFESSIONAL TIMING SERVICE	"Supply/Demand Formula"	13.05	18.27
THE DINES LETTER	Long-Term	12.39	14.76
DOW THEORY LETTERS	Primary Trend	11.05	13.88
THE MUTUAL FUND STRATEGIST	MIRAT-Rydex Growth Portfolio	10.51	12.02
AND EXCHANGE	U.S. Market Timing	9.86	13.25
MARKETARIAN LETTER	Mutual Fund Portfolio for Investors	9.72	10.53
THE PROFESSIONAL TAPE READER	Intermediate-Term	8.95	11.24
FUTURES HOTLINE MUTUAL FUND TIMER	Stock Fund	6.38	7.40
THE ELLIOTT WAVE THEORIST	Investors	5.84	7.17
WILSHIRE 500	VALUE-WEIGHTED TOTAL RETURN INDEX	17.57	

*1988-97

**Returns recalculated as if portfolio had same risk as the Wilshire 5000 Value-Weighted Total Return Index. DATA: THE HULBERT FINANCIAL DIGEST, MORNINGSTAR INC., BUSINESS WEEK



around to other categories such as bonds, foreign stocks, and precious metals. Of the classic timers, the best 10-year performance was 16.9% a year; the worst 4.4%. The average of 24 timers with 10-year records was just 10.9%. The dynamic asset allocators looked better because they had more asset classes to choose from, says *MoniResearch's* Shellans. The best of those managed a 22% average return, the worst 7.0%, and the average 14%.

Why do timers seem so inept? The stock market makes dramatic moves in relatively short periods, and those who miss them effectively miss a lot of the gains. For example, the Standard & Poor's 500-stock index has had an 18.05%

market goes up more than it goes down. So timers, some of whom spend only one-third of their time invested and the rest in cash, end up missing some neat moves. In fact, timers are better at getting out of the market than finding their way back in, says Jim Schmidt, editor of *Timer Digest* (203 629-3503). "The market can jump 4% or 5% after a fall, and the timer will wait to reenter, expecting the prices to come back down. But when prices don't, he ends up buying in at even higher cost or missing the move altogether."

Another reason for the timers' poor results is that they err on the side of bears. One who hasn't is Don Wolanchuk, who was named top timer for 1997 by *Timer*

Timers did well during Wall Street's funk of the 1970s. But through the long bull run, most have badly underperformed the market

America Online, key-3W).

ert's conclusion: None newsletter timers beat market. For the 10 years ended Dec. 31, the timers' average total returns from 16.9% to 5.84%.

During the same period, the Standard & Poor's 500-index earned 18.06% and the Wilshire 5000 Weighted Total Return a broader measure of performance, 17.57%.

OUT. Hulbert and others, however, that raw are not a good way measure timers, since often in cash and thus less exposure to the market's volatility. So we calculated what the timers' records would have been if they taken on the same risk as the Wilshire 5000. On that basis, the timers did better. But their average annual return rose to just —nearly two percent-

age points behind the average U.S. diversified equity fund.

Among newsletters, *Market Logic's* Seasonality Timing System stood out (800 442-9000). It's based on the market's propensity to rise on the last day of the month, the first four days of the next month, and the two days before market holidays. *Market Logic* Editor Norman Fosback, who developed the system, says he invests in selected no-load funds right before those days and exits at the end. The record: about 16% a year for the past 20 years.

Investment managers who mix mutual funds and market timing don't appear much savvier than the newsletter crowd. *MoniResearch* tracks 85 managers with a total of \$10 billion, and divides them into "classic" timers, who are either in equity mutual funds or cash (Treasury bills or money funds), and "dynamic asset allocators," who move assets

average annual return over the past 10 years. But if a market timer had been in Treasury bills during the market's best month, the 10-year average drops by three quarters of a point, says Crandall, Pierce & Co., an investment research firm. Take out the six best months, and the return falls to 12.55%. With small-cap stocks, the moves are more dramatic, and missing the six best months slices the return by 40%.

Downward moves can be swift as well, and one of the allurements of timing is the hope of avoiding them. A 10-year investment in the S&P 500 less the six worst months would boost results to a 22.8% average return, according to Crandall Pierce. Even missing the one worst month hikes returns by nearly one percentage point a year.

But up and down moves aren't a matter of a coin toss. Over long periods, the stock

Digest. Wolanchuk says that except for a few brief periods, he has been bullish for 10 years. According to *Timer Digest*, Wolanchuk's timing returns work out to 20.2% a year for the eight years ending in 1997, vs. 13.5% for the S&P 500. Wolanchuk delivers advice on an \$8,000-a-year hotline or a \$2.75-per-minute 900 number. (For more information, call 800 511-0781.)

Most timers defend their systems as a way to minimize risk. If that's your goal, there are better ways. One method, which is easy with mutual funds, is to diversify into other asset classes such as bonds, foreign equities, and real estate. Another way: Split your portfolio between an S&P 500 index fund and money funds, and rebalance annually. Over the last 10 years, that would have yielded a 12% average return—a good deal better than many timers. *Jeffrey M. Laderman*

HOW TO PLAY THE VIDEO-GAME MAKERS

Video-game execs are as exuberant these days as the kids who play their shoot-'em-ups. Sony's three-year-old PlayStation, along with Nintendo 64, just capped off the hottest video-game season

INVESTING

ever. Market leader PlayStation racked up more than \$2.4 billion in North American sales in 1997, and analysts think the run of good news is nowhere near its end. "We're going to see a longer, more profitable video-game cycle than ever before," says Larry Marcus of BT Alex. Brown.

With all the hype, you'd think now would be a great time to invest in the game biz. But tread carefully. This is a hit-driven industry subject to the fickle cravings of male teens and twentysomethings. Look no further than Sega Enterprises, which has watched sales of its Saturn system disintegrate amid inept software development and poor management. And some analysts wonder if high-speed cable TV or DSL phone modems will spur online gaming and lure video-gamers onto PCs with improved 3-D graphics.

BOTH HANDS. For now at least, gamers aren't ready to abandon PlayStation and Nintendo 64. Indeed, video and PC games have coexisted nicely for years. Even sub-\$100 PCs are far more expensive than \$149 video-game machines, which may fall in price. So one way to get around the PC vs. video-game competition is to invest in software makers that play in both camps. One is Electronic Arts, which develops titles for PlayStation, N 64, and PCs. Known for stellar management, a debt-free balance sheet, and strong de-

velopment teams, EA is expected to post a 22% rise in profits for the fiscal year ending Mar. 30. The increase doesn't reflect last year's acquisition of Maxis, famous for *SimCity*. On Feb. 19, EA jumped 11%, to 44%, on a licensing deal with golfer Tiger Woods. "They've shown a consistent ability to be in front of technology cycles and gain market share," says Arcadia Investment analyst John Taylor.

Some tech watchers are keen on Activision. It's making a push overseas, and its stock has been languishing around 14 despite solid management and healthy earnings. Traders are worried that too big a chunk of Activision's revenues may come from single hits, such as the bloody *Quake II*. But Nick Moore, a portfolio manager at Orbitex Management, believes the stock could reach 25 in a year: "Activision is the one with the most upside leverage."

Midway Games could also be in for gains. The company produces arcade games, then follows up with home versions. It has yet to make a big impact in the PlayStation market, but Mike Wallace of UBS Securities expects the stock, now at 20, to hit 30 within the year on a projected 25% earnings rise (before an extraordinary gain).

Betting on the hardware side of the business is tricky. No company has remained industry champion from one game generation to another. Sony is already starting to slip in Japan, where two PlayStations are sold for every N 64. Sony is said to be working on blueprints for a game machine using digital

video disks that would come out around 2000. Even if you believe in PlayStation's continuing good fortune, the system's hardware and software accounted for only 25% of Sony's group operating income in the quarter ended Dec. 31. To buy its stock, you must also like Sony's other businesses, which happen to be doing nicely at the moment.

NEW DRIVE. Nintendo, meanwhile, plans to unveil in July a disk drive that attaches to N 64 and plays games stored on magnetic optical disks. Nintendo games now come on read-only cartridges, which are more expensive to make and take longer to develop. Masahiro Kubota, an analyst at ING Bank Securities in Tokyo, thinks high prices for the complete N 64 setup—about \$200—could hurt sales. Nintendo American deposits receipts now trade around 11%, down a couple bucks since December, and many analysts push them.

You have to believe in the shots to bet on Sega. True, the company has respected its president, a long-standing arc business, and a well-known brand name, and it vows to

back in U.S. homes with next-generation 128-bit console in 1999. But Sega ADRs are trading at 4%, less than half their level of a year ago. Even if Sega comes with a new console, it will have to persuade software developers to write games for it, a tall order with competing brands going gangbusters. "Until there are dramatic changes in the company, I advise investors to stay away from Sega," says Kubota. Fortunately, there are other ways to play this game. *Edward Baig, with Irene M. K*



Portfolio Winners?

COMPANY	STOCK PRICE*	52-WEEK HIGH	PRICE-EARNINGS RATIO*
ACTIVISION	13 1/2	18 1/2	22
ELECTRONIC ARTS	41 1/2	44 1/2	35
MIDWAY GAMES	19 1/2	26 1/2	15
NINTENDO**	11 1/2	13 1/2	19
SEGA ENTERPRISES**	4 1/4	9 1/4	25
SONY**	87 1/2	103 1/2	22

*Feb.

**Amer. Depositary Receipt

SOURCE: BUSINESS WEEK, COMPILED FROM FINANCIAL MARKETS



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Do you have a life insurance policy or annuity issued by Prudential Life Insurance Co.? The huge mutual insurer recently announced plans to go public, and policyholders—who own the company—can only hope

SMART MONEY

that they will be as fortunate as those at Allmerica Financial. They were awarded stock when the Worcester (Mass.)-based insurer shed its mutual status and did an initial public offering in October, 1995. Since then, Allmerica shares have tripled, netting investors an average annualized return of 57.4%.

Ahead of the Pru conversion—which could take two years to complete—is another widely anticipated deal: the planned conversion of Toronto-based Manufacturers Life Insurance Co. Others that may also go public include Metropolitan Life, Pacific Life Insurance, and John Hancock. Why the rush? The

blurring of boundaries among financial-services providers has stepped up the pace of consolidation in the insurance industry. Companies need access to capital, and public stock can be one of the best currencies around. Shares can also be used as incentive compensation for management to improve performance.

If approved by policyholders, Manufacturers' demutualization should go through in the spring of 1999. Salomon Smith Barney analyst Colin Devine describes Manufacturers as one of the industry's most efficient operators. He figures that even if the insurer's shares go for twice their book value, they will still be a good deal. Equitable and UNUM, two of the biggest insurers to convert to date, now trade at about two and three times book, respectively.

But the latest

Some mutual insurers that are going public look like good bets—but not all

round of conversions may not prove as lucrative for investors as the first. For one thing, Allmerica's timing was impeccable, with its shares issued on the eve of a raging bull market. Moreover, Allmerica's shares were priced at just 64% of book value, due to the company's high costs and slow growth in some product lines. Allmerica moved quickly to streamline and boost sales of hot products such as variable annuities. Its net operating income soared to \$181 million in 1997, up 55% from 1995. In contrast, Prudential's low profitability and legal woes stemming from its life insurance sales practices mean investors may have to be patient to see a payoff from their Pru shares. "That's a big ship to turn around," says Larry Mayewski, an analyst with the A. M. Best insurance company rating service.

STOCK FLIPPERS. Some mutual insurers have sought a hybrid form of public ownership. In 15 states and the District of Columbia, a mutual insurer can set up a holding company owned by policyholders, then sell just under 50% of its stock subsidiary in an IPO (BW—Mar. 2). Policyholders typically get first shot at buying into the IPO at the issue price. One company that took this route is AmerUs Life Holdings.

Still, many pros advise caution about putting money in a mutual holding company. Some insurers favor the structure because the conversion takes less time and money. But because the public owns only a minority stake, takeovers of an underperforming mutual holding company would be difficult. And management may be less responsive than it would be in a fully public entity.

You'll fare best if your insurer launches a pure demutualization because you'll usually receive cash or shares in the new public company. Often, a mutual insurer will raise capital by selling stock in an IPO to outside investors at the same time. In many cases, new shareholders have profited by flipping their stock shortly after the conversion.

If you want to play a conversion game, your best bet is to identify the strongest operators. Sources such as A. M. Best, Moody's Investor Service, and Standard & Poor's can indicate whether a company has been plagued by volatile earnings or is facing business problems. You should also pay close attention to how the insurer intends to use the money raised in an IPO. Plans that are vague or represent a major departure from previous strategy could be a warning sign. "I'd be highly skeptical of companies trying

to reinvent themselves overnight," warns Robert S. Ernst, national director of insurance industry services. With a number of insurers expected to go public, investors should afford to be picky. Amy Ben

Insurers that Converted to Stock

	OFFERING DATE	OFFERING PRICE	CURRENT PRICE*
ALLMERICA FINANCIAL	10/11/95	21	60 ¹⁵ / ₁₆
AMERUS LIFE HOLDINGS	1/28/97	16 ¹ / ₂	33%
EQUITABLE	7/16/92	9	52%
UNUM	11/9/86	5 ¹ / ₂ **	50%

*Feb. 23

**Adjusted for split

DATA: SALOMON SMITH BARNEY

One of the best sounding radios ever made... is back!

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Radio is shown smaller than actual size of 15-1/4" wide x 11-1/4" high x 7" deep.



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STEERING YOUR CAR INSURER TO A FAIR DEAL

The day before Thanksgiving, my beloved 1990 Honda Accord was stolen.

I would soon learn that losing a car to a thief was just the start of my woes. Things really got unpleasant after I called my insurance company.

Although the claims adjusters at my carrier, Geico, were unfailingly polite, the company tried to stiff me. It offered only \$7,159 for a car that cost nearly \$15,000 new—and had only 52,000 miles on it. But I learned I didn't have to take it. I did my homework, including researching used-car prices on the Internet. I found the people at Geico who really make decisions. I was persistent. And in the end, I won a better settlement. "However they come up with

a value, test it," advises Robert Hunter, director of insurance at the Consumer Federation of America.

My problem was that Geico, along with many other insurers, doesn't use standard references, such as the National Automobile Dealers Assn.'s Blue Book, to determine fair market value. Instead, it hires consultants who check ads and talk to used-car dealers. "It gives a more accurate value," insists William Mayer, Geico's assistant vice-president for claims. "Sometimes it can be more than book, sometimes less."

But since these consultants

were on Geico's payroll, I doubted their objectivity. Fortunately, I had time to dicker, since Geico, hoping the car would be found, wouldn't pay for 30 days. First, I went to the Web. Two sites provided powerful ammunition. Kelley Blue Book (www.kbb.com) and



Edmund's (www.edmunds.com) get prices by checking dealers and reviewing ads and other sources. Plug in your make, model, year, mileage, and options, and they instantly give you the dealer's retail price. Kelley priced a comparable '90 Accord at \$10,775. Edmund's came up with \$9,956.

Next, I asked Geico to send me its consultant's report. The 16-page printout was based on local ads and the prices of three cars on Washington-area dealer lots. These were supposed to be comparable to mine, but the only '90 Accord they found

had 114,000 miles on it. The list price was \$6,500, but Geico's "take" price—what it felt the car would actually sell for—was only \$5,000. In fact, while the three cars had very different asking prices, the consultants figured the sales price of each by simply knocking \$1,500 off list. Geico also admitted the cars were never test-driven or inspected to see if they had been in accidents. After adding an adjustment to reflect the mileage difference between my car and the 114,000-mile car, Geico made its offer.

Once I saw Geico's proposal, I checked dealers and read classifieds. I found one '90 Accord, with about 60,000 miles, for \$8,995. It seemed like a good starting point for negotiations. I faxed Geico my research, then worked my way up the bureaucratic chain.

BIG STICK. The first guy said he was only authorized to add \$300. His boss ponied up a few hundred more. Since Geico wouldn't pay until we agreed on a settlement, it would have happily negotiated for-

ever. But I needed a car. So I made a final offer: I would take what Geico gave me. But I warned that its offer would have to satisfy the Maryland insurance commission, since I was going to

INSURANCE

send it the whole file for review. Regulators are often industry lapdogs, but insurers still hate to deal with them. And what do you know? The offer went up again. In the end, I got \$8,315—less than the car was probably worth, but \$1,156 more than Geico's first offer. At least I felt I was robbed only once. *Howard Gleckman*

FUND WATCH

■ **NEW FACE.** Sometimes good funds go unheralded for arbitrary reasons. Although the portfolio underlying STI Classic Small Cap Equity Fund opened in 1994, a change in its name and structure last year makes it appear in many databases to be just one year old, a period too short to draw much attention. Yet in the three years ended Dec. 31, the \$369 million fund posted an annual average total return of 32.6%, vs. the 22.4% recorded by the Russell 2000 small-cap index. BUSINESS WEEK Senior Writer Robert Barker spoke with fund manager Brett Barner:



Q: What is your fund's focus?

A: It's a small-cap value approach. The thing that sets us apart is we require a dividend yield from all the securities.

Q: What have you bought lately?

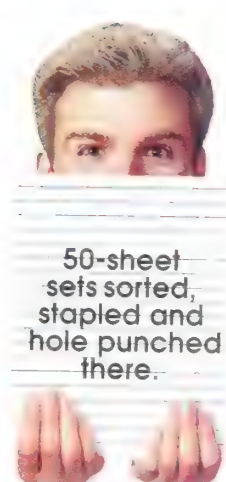
A: Norrell, the temp-services firm. They announced they were going to miss [analysts' earnings estimates for] the quarter. The stock got clobbered. To me, it's a 14-month flu.

Q: What about Sotheby's Holdings? Do you expect a takeover?

A: That's always overhanging, but I wouldn't say I'm in Sotheby's [that]. The art business which has been in a slump since the early is picking up.

For an expanded version, go to www.businessweek.com/totem.htm or AOL, keyword: BW

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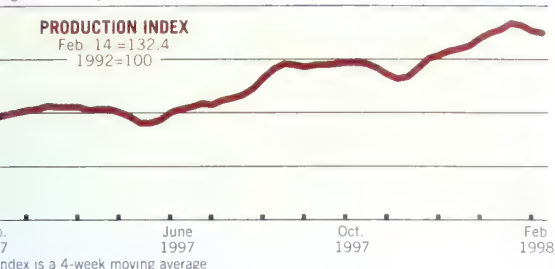
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Business Week Index

PRODUCTION INDEX

Change from last week: -0.2%
Change from last year: 6.4%



The production index slipped slightly in the week ended Feb. 14. However, calculation of the four-week moving average, the index bounced back, to 132.2, from 130.9 in the previous week. On a seasonally adjusted basis, output of steel, autos, trucks, and crude-oil increased. Output of electric power declined again as warm weather lessened the demand for energy.

Production index copyright 1998 by The McGraw-Hill Companies.

LEADING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
PRICES (2/20) S&P 500	1034.21	1020.90	29.0
RATE BOND YIELD, Aaa (2/20)	6.71%	6.69%	-9.1
PRICED MATERIALS PRICES (2/20)	95.4	95.7	-12.3
SUPPLY, M2 (2/9) billions	\$4,081.1	\$4,079.0	6.0
CLAIMS, UNEMPLOYMENT (2/14) thous.	301	303	-1.6
SALES APPLICATIONS, PURCHASE (2/20)	250.8	222.5	22.2
SALES APPLICATIONS, REFINANCE (2/20)	2,005.6	1,685.7	260.7

Sources: Standard & Poor's, Moody's, *Journal of Commerce* (Index: 1990=100), Federal Reserve, Labor Dept., Mortgage Bankers Assn. (Index: March 16, 1990=100)

INTEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
BANK FUNDS (2/24)	5.49%	6.00%	5.28%
COMMERCIAL PAPER (2/24) 3-month	5.45	5.45	5.39
CERTIFICATES OF DEPOSIT (2/25) 3-month	5.56	5.53	5.35
FIXED RATE MORTGAGE (2/20) 30-year	7.10	7.20	7.74
ADJUSTABLE RATE MORTGAGE (2/20) one-year	5.71	5.76	5.65
LIBOR (2/20)	8.50	8.50	8.25

Sources: Federal Reserve, HSH Associates, Bloomberg Financial Markets

Data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

FINANCIAL INCOME

Friday, Mar. 2, 8:30 a.m. EST ▶ Incomes rose 0.6% in January, while consumer spending rose 0.3%, says the median forecast of economists polled by Standard & Poor's International, a unit of The McGraw-Hill Companies. In December, income rose 0.4%, and spending was up 0.3%.

CONSTRUCTION SPENDING

Friday, Mar. 2, 10 a.m. EST ▶ Building spending probably rose 0.5% in January, after a 0.1% advance in December.

SURVEY

Friday, Mar. 2, 10 a.m. EST ▶ The National Association of Purchasing Management's

index in February most likely was unchanged from January's 52.4% reading.

NEW SINGLE-FAMILY HOME SALES

Tuesday, Mar. 3, 10 a.m. EST ▶ New homes probably sold at an annual rate of 802,000 in January, up from 777,000 in December.

LEADING INDICATORS

Tuesday, Mar. 3, 10 a.m. EST ▶ The Conference Board's index of leading indicators is likely to have increased 0.1% in January, after no gain in December.

FACTORY INVENTORIES

Thursday, Mar. 5, 10 a.m. EST ▶ Inventories probably fell 0.2% in January, after slipping

0.1% in December. Factory output rose only modestly in January.

EMPLOYMENT

Friday, Mar. 6, 8:30 a.m. EST ▶ The MMS forecast expects that nonfarm payrolls grew by 250,000 in February, on top of a surprisingly large gain of 358,000 in January. The strong demand for labor is suggested by the low level of jobless claims. The jobless rate most likely remained at 4.7%.

INSTALLMENT CREDIT

Friday, Mar. 6, 3 p.m. EST ▶ Consumers probably added a modest \$5 billion in new debt in January, after borrowing an extra \$3.9 billion in December.

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (2/21) thous. of net tons	2,282	2,232#	8.2
AUTOS (2/21) units	120,475	116,797r#	9.2
TRUCKS (2/21) units	139,888	139,968r#	5.8
ELECTRIC POWER (2/21) millions of kilowatt-hrs.	62,699	64,408#	2.7
CRUDE-OIL REFINING (2/21) thous. of bbl./day	13,805	13,996#	2.9
COAL (2/14) thous. of net tons	22,423#	21,027	7.7
LUMBER (2/14) millions of ft.	479.9#	471.1	-6.6
RAIL FREIGHT (2/14) billions of ton-miles	27.6#	26.5	3.0

Sources: American Iron & Steel Institute, *Ward's Automotive Reports*, Edison Electric Institute, American Petroleum Institute, Energy Dept., WWPAl, SFPAl, Association of American Railroads

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (2/25) \$/troy oz.	292.250	298.150	-17.6
STEEL SCRAP (2/17) #1 heavy, \$/ton	140.50	140.50	-3.4
COPPER (2/20) ¢/lb.	78.0	79.4	-32.4
ALUMINUM (2/20) ¢/lb.	70.3	72.0	-7.6
COTTON (2/20) strict low middling 1-1/16 in., ¢/lb.	62.89	64.41	-11.9
OIL (2/24) \$/bbl.	15.33	15.41	-25.0
CRB FOODSTUFFS (2/24) 1967=100	220.51	224.01	-8.2
CRB RAW INDUSTRIALS (2/24) 1967=100	299.18	299.21	-13.6

Sources: London Wednesday final setting, Chicago market, *Metals Week*, Memphis market, NYMEX, Commodity Research Bureau

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (2/25)	128.65	126.29	120.60
GERMAN MARK (2/25)	1.82	1.82	1.69
BRITISH POUND (2/25)	1.64	1.64	1.63
FRENCH FRANC (2/25)	6.09	6.10	5.71
ITALIAN LIRA (2/25)	1793.5	1796.0	1688.9
CANADIAN DOLLAR (2/25)	1.42	1.43	1.37
MEXICAN PESO (2/25)	8.573	8.531	7.950
TRADE-WEIGHTED DOLLAR INDEX (2/25)	109.6	109.6	104.3

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars. Trade-weighted dollar via J.P. Morgan

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ONLINE

BusinessWeek

Monday

Family problems can be disastrous to a family business. But James Hunt, management professor at Babson College, has come up with ways to keep this from happening. **Mar. 2 8 p.m. ET in the BW Enterprise Chat Room**

Thursday

What's the best strategy for finding the best stocks? Bring your questions to Robert S. Natale, vice-president and director of equity research at Standard & Poor's, and BW's Jeffrey M. Laderman. Meantime, check out Jeff on market-timing in this issue. **Mar. 5 9 p.m. ET in the BW Online Conference Room**

AOL keyword: BW Talk

Transcripts of all conferences are available for downloading from the BW Online area on AOL soon after each event



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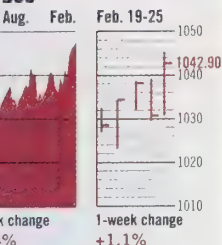
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Investment Figures of the Week

KS

500



CENTURY

equity market's version of
trick: On Feb. 25, inflows
stock mutual funds helped
Dow Jones industrial aver-
Standard & Poor's 500-
index, and the NASDAQ
posite all rack up new
The tech-heavy NASDAQ
the most and is up 12.5%
year. Investors brushed
Federal Reserve Chairman
Greenspan's cautionary
ings about whether turmoil
a would check inflation-
dependencies in the U.S. Re-
ing Asian markets made
region's equity funds lead-
four-week total return.

U.S. MARKETS

	Latest	% change Week	Year
Dow Jones Industrials	8457.8	0.1	21.1
NASDAQ Combined Composite	1766.5	3.0	31.8
S&P MidCap 400	350.1	1.0	31.4
S&P SmallCap 600	192.7	1.4	32.0
S&P SuperComposite 1500	223.8	1.1	29.7

SECTORS

	Latest	% change Week	Year
Bloomberg Information Age	330.9	2.5	33.8
S&P Financials	125.5	1.1	33.2
S&P Utilities	232.3	0.2	18.2
PSE Technology	337.0	2.3	27.1

FOREIGN MARKETS

	Latest	% change Week	Year
London (FT-SE 100)	5745.1	0.4	32.7
Frankfurt (DAX)	4635.8	0.2	43.2
Tokyo (NIKKEI 225)	16,360.6	-1.5	-13.9
Hong Kong (Hang Seng)	10,886.7	2.0	-19.6
Toronto (TSE 300)	7002.1	0.8	12.9
Mexico City (IPC)	4740.2	4.2	21.9

FUNDAMENTALS

	Latest	Week ago	Year ago
S&P 500 Dividend Yield	1.48 %	1.51 %	1.79 %
S&P 500 P/E Ratio (Last 12 mos.)	25.2	26.1	21.2
S&P 500 P/E Ratio (Next 12 mos.)*	20.1	20.1	17.2
First Call Earnings Revision*	-2.77 %	-3.43 %	-0.71 %

TECHNICAL INDICATORS

	Latest	Week ago	Reading
S&P 500 200-day average	934.9	929.6	Positive
Stocks above 200-day average	65.0 %	66.0 %	Neutral
Options: Put/call ratio	0.54	0.55	Negative
Insiders: Vickers Sell/buy ratio	1.56	1.58	Positive

Data: Bloomberg Financial Markets; *First Call Corp.

BEST-PERFORMING GROUPS

	Last month %	Last 12 months %
HMOs	28.4	Specialty Appar. Retailers 85.3
Machine Tools	27.0	Broadcasting 73.1
Conglomerates	21.0	Airlines 67.5
Engineering & Constr.	20.6	Manufactured Housing 66.3
Personal Loans	20.6	Homebuilding 66.2

WORST-PERFORMING GROUPS

	Last month %	Last 12 months %
Gold	-9.3	Gold -40.8
Tobacco	-3.5	Metals -40.5
Pollution Control	0.1	Shoes -38.6
Regional Telephone Cos.	0.3	Engineering & Constr. -27.7
Long-Dist. Telecomm.	0.4	Photography/Imaging -24.8

BLOOMBERG MONEY FLOW ANALYSIS

Rebound ahead? Stocks with most significant buying on price weakness

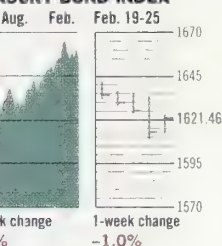
	Price	1-month change
Sun Microsystems	44 7/16	-9 1/16
AMR	124 3/8	-1/2
BellSouth	59 1/16	-3/8
American Home Products	89 11/16	-13/16
SBC Communications	75 1/8	-13/16
Dow Chemical	87 3/16	-39/16

Decline ahead? Stocks with most significant selling on price strength

	Price	1-month change
Microsoft	82 1/8	11 1/4
Cisco Systems	64 3/4	8 1/8
Intel	92 3/8	14 11/16
Dell Computer	128 7/16	33 11/16
Oracle	26 3/16	7 1/4
WorldCom	37 15/16	4 15/16

REST RATES

TREASURY BOND INDEX



Bloomberg Financial Markets

KEY RATES

	Latest week %	Week ago %	Year ago %
MONEY MARKET FUNDS	5.14	5.16	4.95
90-DAY TREASURY BILLS	5.29	5.20	5.22
6-MONTH BANK CDS	5.03	5.09	5.01
1-YEAR TREASURY BILLS	5.40	5.27	5.64
10-YEAR TREASURY NOTES	5.61	5.49	6.56
30-YEAR TREASURY BONDS	5.92	5.84	6.80
LONG-TERM AA INDUSTRIALS	6.54	6.46	7.28
LONG-TERM BBB INDUSTRIALS	6.95	6.91	7.61
LONG-TERM AA TELEPHONES	6.83	6.74	7.48

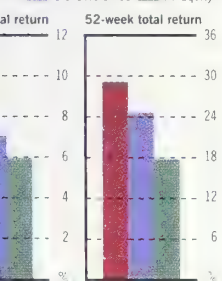
BLOOMBERG MUNI YIELD EQUIVALENTS

Taxable equivalent yields on AAA-rated, tax-exempt municipal bonds, assuming a 31% federal tax rate.

	10-yr. bond Latest week	30-yr. bond Latest week	Latest week	Last week
GENERAL OBLIGATIONS	4.35%	4.28%	4.94%	4.86%
PERCENT OF TREASURIES	77.52	78.11	83.48	83.34
TAXABLE EQUIVALENT	6.30	6.20	7.16	7.04
INSURED REVENUE BONDS	4.47	4.41	5.15	5.08
PERCENT OF TREASURIES	79.66	80.48	87.05	87.11
TAXABLE EQUIVALENT	6.48	6.39	7.46	7.36

MUTUAL FUNDS

0** U.S. Diversified All Equity



Morningstar, Inc.

EQUITY FUNDS

Leaders	Laggards
Four-week total return %	Four-week total return %
Guinness Flight Asia Sm. Cap 27.6	Prudent Bear -13.3
U.S. Global Inv. China Reg. 25.7	U.S. Global Investors Gold -12.3
Colonial Newport Gr. China A 25.7	Rydex Precious Metals -11.5
DFA Pacific Rim Small Co. 25.5	Lexington Strat. Invmnts. -11.0
Montgomery Emerg. Asia R 23.2	PIMCo Precious Metals A -10.3
Leaders	Laggards
52-week total return %	52-week total return %
Munder Micro-Cap Equity Y 64.5	Midas -62.9
Delaware Aggressive Gr. A 56.4	U.S. Global Investors Gold -62.9
Texas Capital Val. & Gr. 53.2	Bull & Bear Gold Investors -60.7
MFS Strategic Growth A 52.2	Invesco Strategic Gold -60.1
Fidelity Sel. Air Trans. 52.0	Gabelli Gold -54.5

EQUITY FUND CATEGORIES

Leaders	Laggards
Four-week total return %	Four-week total return %
Pacific/Asia ex-Japan 13.6	Precious Metals -6.7
Technology 12.2	Japan -3.8
Mid-cap Growth 8.7	Real Estate -0.9
Small-cap Growth 8.3	Utilities 1.3
Large-cap Growth 8.1	Natural Resources 1.6
Leaders	Laggards
52-week total return %	52-week total return %
Financial 35.1	Precious Metals -46.4
Communications 32.0	Pacific/Asia ex-Japan -35.9
Unaligned 29.4	Diversified Pacific/Asia -26.3
Small-cap Value 28.1	Diversified Emerging Mkts. -15.9
Large-cap Growth 27.4	Japan -10.4

as of market close Wednesday, Feb. 25, 1998, unless otherwise indicated. Industry
include S&P 500 companies only. Fundamentals, technical indicators, Bloomberg mon-

ey flow analysis, and mutual fund returns are as of Feb. 24. For a more detailed explanation, write
to us or E-mail figures@businessweek.com. NA=Not available **Vanguard Index 500 Fund

JAPAN NEEDS TO FACE THE MUSIC—NOW

Japan's economic decline is a sad spectacle of denial and defiance. Once a model to emulate, the Japanese economy is now the subject of derision. Once the fastest-growing industrial nation, Japan is now the slowest. Strong corporations remain powerful global players, but the Japanese economy is caught in a vicious downward cycle of shrinking activity, shattered consumer confidence, and ineffective government policies. Just when Japan should take the lead in helping Asia recover, it is part of the problem, not the solution.

A veritable chorus of top Asian, European, and American officials are asking Tokyo to change policies. Malaysia, which built its prosperity on a closed Japanese mercantilist model, is now pleading for Tokyo to deregulate and open its markets to imports from the rest of Asia. At the recent G-7 meeting, Germany, France, and Britain joined the U.S. in an unprecedented public request for Japan to cut taxes to raise consumption, boost domestic-led growth, and buy more from Korea, Thailand, and Indonesia. A confidential study by the International Monetary Fund states that Japanese officials have done too little too late.

Japan's response so far? It denies responsibility. In fact, Japan dramatically changed the terms of trade in Asia by allowing the yen to plummet. It chose to promote exports rather than stimulate its economy and absorb imports. The move followed China's devaluation, putting the rest of Asia in a pincer that set the stage for the current crisis. The competitive devaluations backfired. This January, Japan's exports to Korea were down 42% from a year earlier, and exports to Thailand and Malaysia were off 35% and 16%, respectively.

Japan also has been in denial about its own economic malaise for nearly seven years. Despite prodding by the U.S. and others to deregulate its economy and cut taxes to boost consumption, it has relied on its old mercantilist faith in the magic of a trade surplus. Yet a foreign exchange policy that has weakened the yen by nearly 40% has failed to increase growth.

What may be holding back Japan the most is an obsession with the care and feeding of its aging population. The sacrosanct, centralized, bureaucratically run system designed to concentrate and funnel savings into production is now channeling them into retirement. Tokyo is raising taxes to get its fiscal house in order and is dragging its feet on deregulation for fear of unleashing costly unemployment on its older workers. Economic anxiety is, in turn, leading people to save even more and spend less, further dampening growth. What is surely a noble goal is turning into an economic nightmare.

All the industrialized countries face the same problem. In the U.S. is now discovering, high economic growth accelerates the Social Security and Medicare burden caused by aging baby boomers. But Japan is unwilling to chance reform and take the high-growth solution. Instead, it is mistakenly choosing no-growth policies.

The transformation of one of the most dynamic economies in recent history into a defensive, stagnant caretaker society is a tragedy of immense proportions. For years, Japan's stubborn unwillingness to cut taxes and deregulate led to chronic trade friction with the U.S. Now, it has undermined Asian prosperity, and its own.

THE EURO MAKES TRADE A NEW GAME

Get ready for the protectionist Cassandras to begin shouting their alarms in the months ahead. The trade deficit, because of the Asian crisis, is set to explode. As Asia drops into recession, it may peak out at \$300 billion.

There is no cause for panic over this short-term bulge in the U.S. deficit (page 30). The American economy is nearly twice as large as it was in 1987, the last time the deficit loomed as a problem. As a percentage of gross domestic product, the deficit, at its worst, will be smaller than a decade ago. U.S. companies are also far more competitive now. Exports were extremely strong before Asia hit the wall and will be stronger still in the future. Exports to Mexico are at record levels, two years after that country's financial crisis. Market openings, and financial reforms mandated by the International Monetary Fund, will produce record U.S. exports to Korea, Thailand, and other Asian countries a year or two down the road.

But there is no room for complacency. Thanks to the dollar's role as reserve currency in world financial markets, the U.S. has been able to do what no other country can—con-

sistently import more goods than it exports. Dollar hegemony has raised America's standard of living beyond what it could otherwise attain. People hold the dollar overseas because it is a good store of value and because there is no alternative. Until now, that is. Soon a competing numeraire, the new euro, will make its appearance. And Europe's single currency could make it much harder for America to continue running current-account deficits. Germany and France fully intend to make the euro a reserve currency. They see it as the financial equivalent of Europe's Airbus Industrie, the only major competitor anywhere to the U.S.'s Boeing Co.

The U.S. owes some \$5 trillion to dollar holders abroad thanks to three decades of trade deficits. This "dollar overhang" hasn't been a problem to date. But by 2001, the competing store of value to the dollar since the days of the strong pound sterling will be here. No one knows what will happen. But though the impending surge in the trade deficit poses no immediate threat, America should ponder getting its trade house in order. The euro could change everything.

BusinessWeek

March 16, 1998

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VALLEY TO HILL

The titans of high tech head east to have their

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COVER STORY

ON THE EDGE

China's economy is wobbling, and a major shift in policy toward public spending is about to change history page 44



BusinessWeek

MARCH 16, 1998

Cover Story

44 CAN CHINA AVERT CRISIS?

As the economy starts to sputter, planners are hitting high gear. Reforms pegged to austerity are history. Something new is desperately needed. Inflation—and social unrest—wait in the wings. Envisioned is a massive public-works program. But with a dysfunctional banking system and an untested leadership, will it work?

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Silicon Valley's big-time entrepreneurs can no longer pretend that Washington is irrelevant—and vice versa

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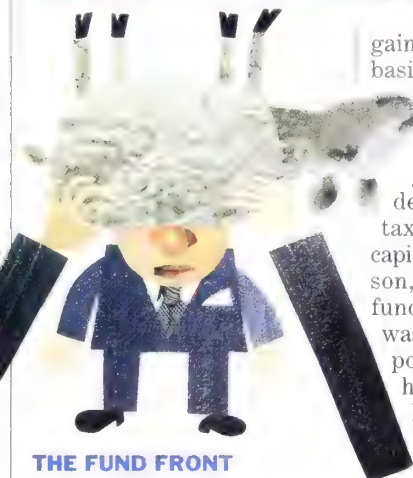
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Up Front

EDITED BY ROBERT McNATT & LARRY LIGHT



THE FUND FRONT

THAT FINE PRINT CAN BURN YOU

EVERY INVESTOR LOVES A TAX break. But at Charles Schwab, one break may not be quite as good as it seems. In a print ad for its Schwab 1000 Fund, which holds stock in the 1,000 largest public companies, Schwab extolls the fund's "tax efficiency." It prominently notes that for seven years the fund has distributed no taxable capital

gains: As an index fund, it basically buys and holds.

What the ad doesn't explicitly say, however, is that the fund still generates small dividends, which are usually taxed at a higher rate than capital gains. Michelle Swenson, Schwab's top mutual-fund marketer, says there was no intention to mislead potential investors. "It hadn't occurred to anyone here," she says. "When Chuck [Schwab] talks about tax efficiency, he's talking about capital gains." The ad also satisfied the National Association of Securities Dealers, which checks mutual-fund ads. It declined to comment.

Swenson says she'll review the ad and make fixes, if needed: "Maybe we can do this with a footnote." Perhaps it would note that Morningstar says the fund's average annual pretax total return from 1992-97 was 19.1%, but dropped to 18.6% after taxes. *Jeffrey Laderman*

TINSELTOWN

LIGHTS! CAMERA! DEATH STICKS!

REMEMBER KATE WINSLET and Leonardo DiCaprio in *Titanic*, lighting up before the ship went down? How about Sharon Stone puffing away in *Dia-bolique* with those dark glasses on?

Maybe nobody in Hollywood ever read the Surgeon General's warning. Only 14% of Americans now smoke. But there has been a big upswing in movie smoking in the '90s, says Stanton Glantz and Theresa Stockwell, researchers at the University of California at San Francisco. In a study published in the



THE LOOK: Stone

journal *Tobacco Control*, they monitored smoking in top-grossing films since 1960. Someone smoked about once for every five minutes of film time in the 1960s. In the 1970s and 1980s, the rate dropped to once every 10-15 minutes. But in the backsliding '90s, characters light up as often as every three minutes.

And in films released from 1991 to 1996, the researchers say 57% of all leading characters smoked.

Glantz can't explain the increase, but he says that "tobacco use in the movies is associated with youthful vigor, good health, good looks." Joe Camel may be retired, but his legacy lives on in Hollywood. *Catherine Arust*

TALK SHOW "We felt that a lot of rights have eroded in this country. Our freedom of speech may be the only one we have left to regain what we've lost."

—Juror Pat Gowdy after Texas cattle ranchers lost their beef defamation suit against Oprah Winfrey

FWAY PATROL

A WEB SITE FOR SORE EYES

CBS GOT LESS THAN STELLAR marks for its Olympic coverage, but its partners at CBS-Sportsline captured a medal for their Web site. They have high hopes of scoring just as big with the NCAA men's basketball tournament.

The four-year-old company that runs the Web site, Sportsline USA, showed a 245% increase in viewership during Nagano, more than any of the other big sports sites.

And according to Relevant-Knowledge, which rates Web viewership, Sportsline was the third-most-watched site, behind No. 1 ESPN SportsZone and the official Olympics site.



NCAA: "Good start"

It also knocked another big site, CNN's, into fourth place. Best of all, Sportsline reaped more than \$2 million in revenue, 40% of its 1997 total from advertisers such as Budweiser and Intel.

Although CBS Sportsline ratings were undercounted, he's optimistic. "We have momentum and CBS picking up NFL is another big plus for us," says Levy. He also says that NCAA basketball is "off to a good start."

While the CBS connection is a major plus for Sportsline, it also runs the home pages for high-profile athletes such as Tiger Woods. *Gail DeGeorge*



CAR TALK

FOR THE DRIVER WHO HAS EVERYTHING

THE BALLERINA FLITTING about, dressed as Rolls-Royce's "Spirit of Ecstasy" hood ornament, may have been overkill. Then again, it's not every day that Rolls-Royce Motor Cars unveils a new make. In fact, there hasn't been a new Rolls for 18 years. Now there is.

The Rolls-Royce Silver Seraph, which debuted at the Geneva motor show on Mar. 3, is a sleekly rounded ode to excess with a base price of about \$255,000. And what, you may ask, does one get

for the price of a dozen Honda Accords? For starters, a sedan with vast expanses of burled walnut and leather. Plus, options such as the \$8,900 dual video monitor with cordless headphones.

The carmaker hopes the Seraph will boost sales, including its Bentleys, to 2,500 cars this year, from 1,900 in 1997. Still, the Seraph reminds Britons that the stately is setting on another piece of the empire. German automakers BMW and Volkswagen have both said they want to buy Rolls from its owner, Vickers PLC, though neither has made a bid yet. So a deal may not be announced until April. *Kathleen Kerwin*

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underscores
results.

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Arrogance
undermines
results.

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Up Front

FOODSTUFF

PROCTER & GAMBLE'S CHIP UPGRADE

CANS OF PROCTER & Gamble's Olestra-made Pringles potato crisps now say that the snacks with the controversial fat substitute have "Amazing Taste." Evidently, though, it's not amazing enough. The consumer-products company will soon begin selling fat-free Pringles made with a new recipe. Or, as P&G says, there will be a "flavor upgrade."

The leap to good taste follows a P&G-sponsored study in the *Journal of the American Medical Assn.* on the effects of Olestra. The study concluded that consumers suffered no higher levels of gastric distress from Olestra-made potato chips than from traditional ones. But it also said consumers didn't like the taste of Olestra



chips as much. The maker of the chips in the study, Frito-Lay, is changing its recipe. Now P&G, which makes

Olestra, is following suit with its fat-free Pringles.

P&G insists that the Olestra potato chip study had no influence in its decision to change the Pringles recipe. It was being fine-tuned prior to the study. The company also says that this isn't even the first time the Pringles recipe has been changed. At any rate, the new Pringles version, says P&G, will appear in selected Midwest markets in March, with a taste that is supposed to be "more potato-ey." That should not be too much to ask of a snack food that is made from potatoes. *Jeff Harrington*

SLUGFESTS

LOOK OUT—BIG BERTHA IS MAD

GOLFERS LOVE PLAYING WITH Big Bertha. That's the hot-selling oversize club made by Callaway Golf that sells for up to \$700. But a golf ball hyped as the perfect match for Big Bertha is being sold by a Callaway competitor, Spalding Sports Worldwide. And that has Callaway so teed off that it is suing Spalding for trademark infringement, false advertising, and unfair competition.

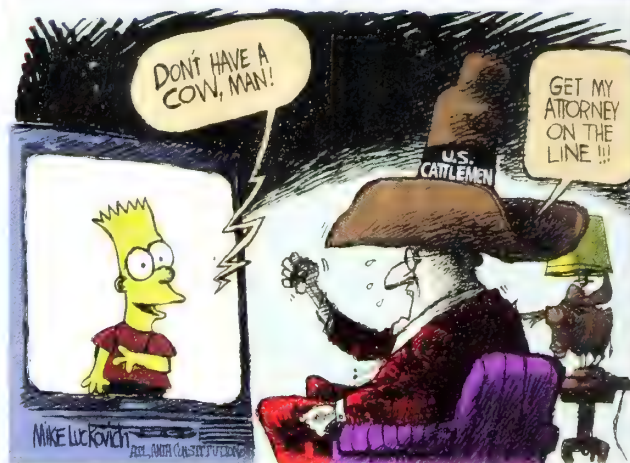
Boxes of Spalding's Top-Flite/Club System C balls, which go for \$54 a dozen, feature a picture of a Callaway club and say the balls will help improve play with Big Bertha drivers. The box

TOP-FLITE
SYSTEM
4

carries a disclaimer noting that the product has no connection to Callaway. But that has failed to satisfy Callaway—largely because it wants to start its own line of Big Bertha balls.

Spalding doesn't care. "We reviewed this packaging thoroughly prior to launching the product," says John Hoagland, a Top-Flite exec. "We have no doubt that it complies with the law, and we are confident the court will agree." Meanwhile, Taylor Made Golf, another company whose clubs are featured on Top-Flite boxes—with a similar disclaimer—has decided to sit out the legal fracas. Taylor also disapproves of Spalding's tactics. Maybe they all should relax—and settle the whole thing with 18 holes of match play. *Dennis Blank*

DRAWN & QUARTERED



SHOW BIZ

THE FILMMAKER IS A THEATER CRITIC

GEORGE LUCAS, THE MAN behind the *Star Wars* and *Indiana Jones* movies, is already one of America's top filmmakers. Now, he is poised to become its top theater cop, too.

For 15 years, THX, a division of Lucasfilm, has made a business of rating 6,500 U.S. theaters for film distributors based on sound and picture quality as well as cleanliness and comfort. Now, the company may make its list of best theaters public through its Internet site—if distributors approve. "We have to make sure there is a benefit to our exhibitors,"

says Marc Spector, head marketing for THX. "But we will trial-balloon it."

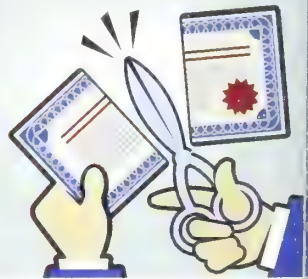
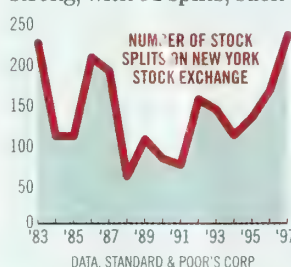
Filmgoers may love the idea, but theater owners are reacting like Darth Vader faced with the Rebel Alliance. "We would have a problem with it," says Phil Zacheret, spokesman for the 2,350-screen Regency Cinemas chain. The problem: The Lucas unit also sells a sound system. "We are you going to judge better: one with your sound system or one without?" Do you sense a disturbance in the Force? *Roy Furchg*



COLD EYE? Lucas

THE BIG PICTURE

DOING THE SPLITS As the market booms, companies are increasingly splitting their stock to make it more affordable. Last year's 235 splits exceeded the previous record, 1983's 225. Thus far in 1998, the pace has stayed strong, with 52 splits, such as Lucent, CIGNA, and Amoco.



FOOTNOTES Percentage of people who say that insurance-claim padding is O.K.: 1993, 22%; 1997, 40%

The New Chrysler Town & Country

We made it exceptionally quiet.
However, it still produces an occasional buzz.



Chrysler Town & Country. "America's Most Appealing Minivan" Two Years In A Row.

—J.D. Power and Associates

For the second year in a row, the Chrysler Town & Country has been honored with J.D. Power and Associates' prestigious APEAL award. In their recent study, Town & Country tied as "America's Most Appealing Minivan" after its owners rated it on over 100 attributes.*

So while we always insist that it be quiet, we certainly don't mind hearing this sort of noise.



*J.D. Power and Associates 1997 APEAL Study—Automotive Performance, Execution and Layout Study "Segment" Compact van. Study based on a total of 29,187 consumer responses.

PUTERS THAT CAN EN AND UNDERSTAND

abled people have great need for ologies that help them gain inde-
ence. As profiled in "Let's talk"
ial Report, Feb. 23), speech tech-
y is one that gives the disabled
s to computers. The Internet has
potential for sharing information
treatment and research. As I
more people who have limited or
e of their hands, I recognize how
al this can be.

Christopher Reeve

Chairman

Christopher Reeve Foundation

New York

T WORKERS WANT A SAY IN NS' POLITICAL GIVING

"Labor and the GOP: A shootout in
rnia" (News: Analysis & Commem-
Feb. 16), you quoted AFL-CIO Pres-
John Sweeney's claim that Propo-
226 is "an attempt by conservatives
business to silence the voice of work-
milies." Yet you did not note that
poll conducted on Prop 226 shows
more than 65% of union members
Democrats support our efforts to
union leaders more accountable on
they spend members' dues on poli-
Prop 226 places the same require-
on employers as it does on unions:
yroll deductions for politics with-
worker's permission.

ile I welcome the support of na-
leaders, Prop 226 proudly wears
bel "Made in California." The idea
e initiative was hatched in my liv-
om.

Mark Bucher

Co-Chairman, Yes on 226!

Tustin, Calif.

REGIONS & CLARIFICATIONS

e tables accompanying "Is this the end
e glory days?" (Corporate Scoreboard,
2), the correct change in Crown Cork
al's 12-month profits was 6%, and the
h-quarter 1996 margin was 2.0%. For
lass, Metal & Plastic industry group,
change in 12-month profits was 32%,
e the fourth-quarter 1996 margin was
e.

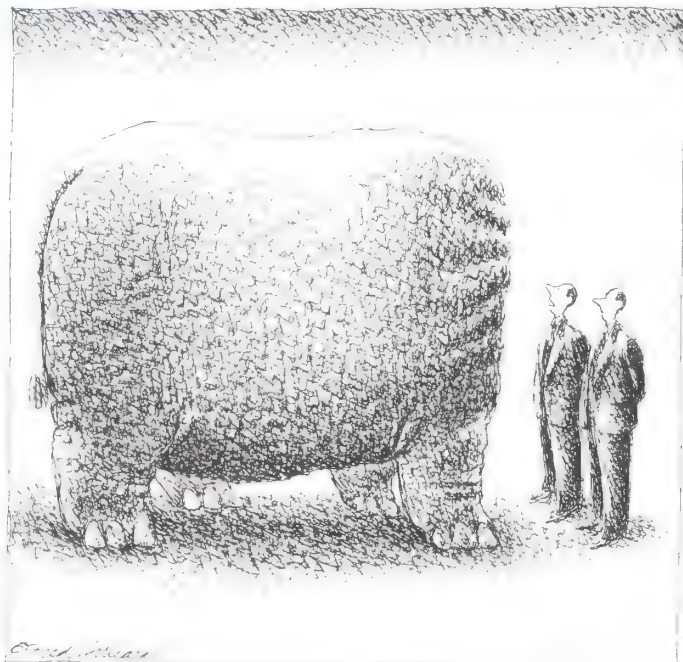
oduction error omitted the byline in
ergency surgery for MedPartners" (Peo-
Mar. 9). The story was written by Nicole
s in Birmingham, Ala., with Anthony
co in New York.

CRAMPING COACH PASSENGERS TO CODDLE FIRST CLASS

Your otherwise informative story
"Airlines raise their class conscious-
ness" (News, Analysis & Commentary,
Feb. 23), was somewhat inaccurate re-
garding TWA. Our airline's main cabins
currently offer passengers 31-inch seat
pitch—which is as much room as any

competitor offers and more room than
many. We formerly provided two or
three additional inches between the
rows in coach class. We've moved that
space up front to add 60% more first-
class seats in our domestic cabins. This
gives business travelers more oppor-
tunities than with any other airline to
reserve or upgrade into a first-class
seat. Business fare travelers pay more

WillTales



*"Boy! This thing's been wandering around
for quite a while. Which reminds me...
have we notified the Big Phone Company
we're going with that Williams network?"*

that **Williams** network

11,000 fiber miles laid, lit and ready to ride.



Readers Report

and, because of that, think they deserve more. We agree.

Mark E. Abels
Vice-President
Corporate Communications
Trans World Airlines Inc.
St. Louis

The airlines' strategy of coddling first-class passengers at the expense of econ-

omy class is, as usual, a false strategy designed to maximize their short-term profits at the expense of long-term growth.

The willingness of businesses to pay the first-class premium will shrink at the first sign of economic slowdown. The airlines' future growth potential is increasing economy-class travel among the evergrowing population of leisure-rich retirees. Meanwhile, the constant improvement in electronic communications will continue to reduce the demand for business travel.

Thomas T. Semon
Englewood Cliffs, N.J.

COMMON ED LOOKS ON THE BRIGHT SIDE

Regarding "The scramble to keep Commonwealth Edison aglow" (News: Analysis & Commentary, Feb. 23), Commonwealth Edison's residential rates for electrical power compare favorably with those of other major metropolitan areas such as New York and Los Angeles. Over the last five years, it has devoted considerable resources to ensure customers have electricity when they need it. In 1999, when commercial and industrial customers begin exploring an open

market, Commonwealth Edison will be poised to compete for their business, as well as opportunities in other energy-related service.

John T. Costello
Vice-President
Corporate Relations
Commonwealth Edison
Chicago

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Business Bulletin

Patho TEK Cures Common Cold

COLD CURE IN A BOTTLE, developed by Patho TEK, is due for release in mid April.

CoryzaCC will suppress, and in completely wipe out, the symptoms of the common cold.

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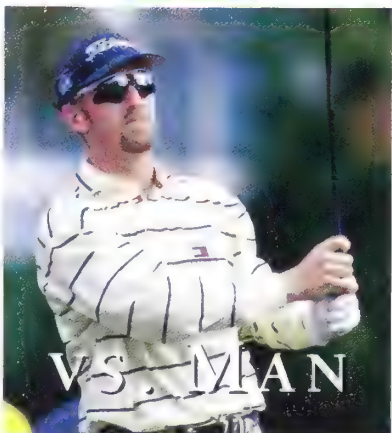
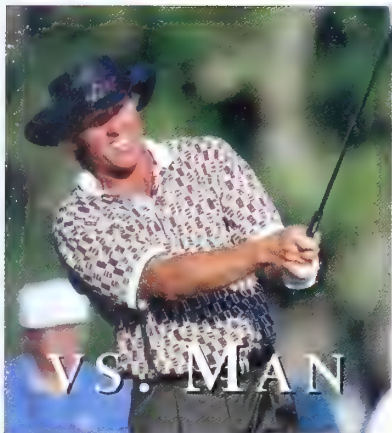
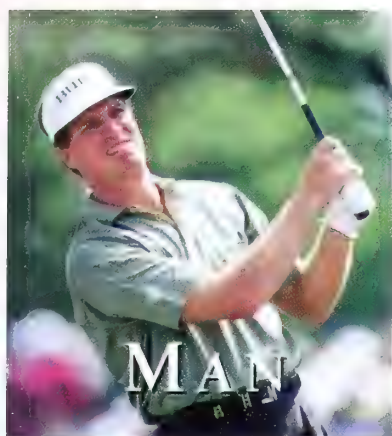
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THESE GUYS ARE GOOD.



PRESCRIPTION FOR DISASTER

The Hidden Dangers in Your Medicine Cabinet

By Thomas J. Moore

Simon & Schuster • 271pp • \$25

WHEN THE CURE MAY MAKE YOU SICKER

Of the 50 top-selling prescription drugs, only four are "safe," says Thomas J. Moore, a medical writer and senior fellow in health policy at George Washington University Medical Center. Numerous others, he claims, can cause addiction, cancer, or heart problems. And the number of Americans killed by pharmaceuticals is quadruple the number of people who are murdered and double the number who die in car crashes. Moore says at least a million each year are "severely injured" by their medications. An additional 2 million are harmed by drugs administered during hospital stays.

Moore, the author of three previous books critical of medical practice, makes all of the above claims in *Prescription for Disaster: The Hidden Dangers in Your Medicine Cabinet*. The claims are backed up with references to studies conducted by the U.S. Food & Drug Administration and others. Moore's goal is to make the public less complacent about prescriptions—and less eager to embrace the cult of the magic bullet. *Prescription for Disaster* does make a compelling case that medications ranging from heart drugs to antipsychotics and pain relievers can do as much harm as good. But Moore neglects a serious discussion of how much risk is acceptable when people are ill and the medicine in question might help them. How many of the people injured by drugs would have died otherwise? Moore sometimes uses figures disingenuously to make his points. But he raises important issues about drug safety.

A key problem, according to Moore, is that there is no effective oversight of drugs already on the market. "To monitor the safety of 3,200 approved drugs...the Food & Drug Administration has a staff of just 54," he writes. This effort receives just 4% of the FDA budget for drug evaluation—less than \$5

million. Doctors are supposed to report deaths or serious injuries caused by prescription drugs. But Moore notes that only about 1% of serious events are reported, according to former FDA Commissioner David A. Kessler. Moreover, Moore says, the pharmaceutical industry has a strong motive for keeping the public in the dark: Public worries about drug dangers "might interfere with the relentless drive to sell ever larger numbers of drugs."

Moore also takes aim at doctors who don't tell patients about side effects or who prescribe drugs merely because patients demand them. An FDA survey found that 70% of patients studied were not told about side effects. Injuries can occur when pharmacists don't notice harmful drug combinations or when they fail to provide labeling information. And finally, Moore assigns blame to patients who don't ask about the drugs they are taking or who use them inappropriately.

Moore notes that drugs have benefits, too. Few people think of chemotherapy drugs as safe; yet their beneficial effects against cancer make the risk acceptable. The same is true of drugs for AIDS or serious bacterial infections. Moore's arguments are strongest when the advantages of long-term use are either very small or unclear.

Because so many people take prescription drugs, a small risk of dangerous side effects can translate into tens of thousands of injuries. Citing FDA calculations, Moore says that Eli Lilly & Co.'s Prozac, for example, "was associated with more hospitalizations, deaths, or other serious adverse reactions reported to the FDA than any other drug in America."

Drugs may win approval following clinical trials of a few months involving controlled populations of several hundred people. But later, surprises do occur. To detect these problems, the FDA relies on doctors' voluntary reports—a seriously deficient approach, write Moore. As an example, he cites a study of doctors in Rhode Island: The doctors' files show 26,000 adverse reactions to drugs, but only 11 of these were reported to the FDA.

Even when the government issues warnings, doctors don't always heed them, says Moore. Problems with the sleeping pill Halcion, including aggressive behavior and psychosis, prompted the FDA to request that the drug not be prescribed for longer than 7 to 10 days. But a 1996 FDA report found that 85% of prescriptions were for longer periods. The FDA could do nothing; once a drug is approved, doctors are allowed to use it as they see fit.

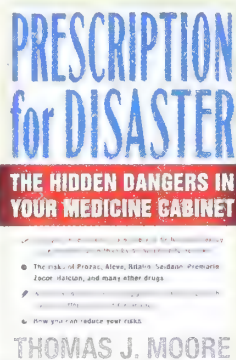
It's hard to argue that society hasn't profited greatly from modern medicine, but it's also clear the system needs help. To that end, Moore offers several worthy proposals, although they may be difficult to enact when Congress is looking to cut taxes and regulations, not expand them. First, he calls for beefed-up FDA surveillance system. Drugs should be reevaluated every five years, and the reporting of adverse effects by doctors

should be mandatory. Companies should be required to do long-term studies on some drugs, using money from a tax on companies that market highly profitable drugs.

Other suggestions include a standard rating system for drug toxicity and, employing the resources of managed-care companies, better oversight of doctor prescriptions. Finally, there's a primer on how to read drug labels and how best to make informed decisions—in concert with a physician—about whether a drug is necessary. From Moore's point of view, prescription drugs represent a double-edged sword. His final advice: Respect that force and use it wisely.

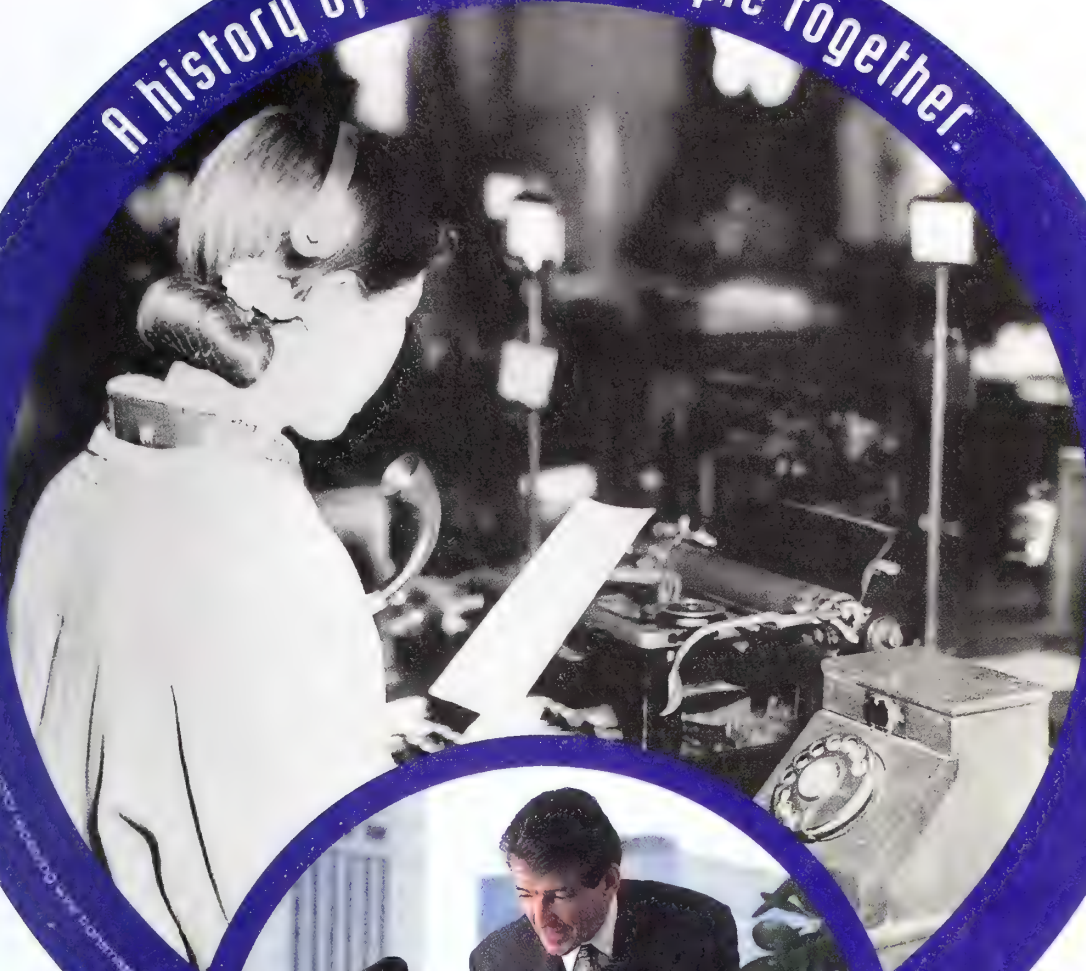
BY NAOMI FREUNDLIC

Freundlich has written extensively on health-care issues.



IN ONE STUDY, DOCTORS NOTED 26,000 ADVERSE DRUG REACTIONS BUT REPORTED ONLY 11

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BY STEPHEN H. WILDSTROM

DESKTOP POWER, LAPTOP SIZE

A choice for those who want to save space without spending a fortune

Personal computers have become standard fixtures in just about every executive office. But many execs don't really want a big PC dominating their desktop. That, as much as the need for mobility, is driving a lot of people to pick a laptop as their primary computer.

Now there's another choice for folks who want the small desktop footprint of a notebook without the cramped keyboard and other limitations—or the steep cost. The Fusion OneBox from Akia (800 936-5481 or 512 339-4804) is an intelligently designed package, starting at \$2,999, that combines a notebook-style, flat-panel display with miniaturized PC built in. The package, which is being sold by phone and on Akia's Web site (www.akia.com), takes up just a 7½-in.-by-11-in. space on your desk, plus room for a compact keyboard and mouse. This is no more than is needed for a laptop with a desktop keyboard and mouse, and a great deal less than required for laptops with docking stations that permit you to hook up to a conventional monitor and keyboard.

True, the Fusion sacrifices portability. It weighs just under 20 pounds and has a handle for easy carrying, but it's

more luggable than portable and needs AC power. It still offers a number of advantages over a laptop.

To start with, there's the display, which is available in a freestanding version for use with standard PCs at \$1,399. The 14.5-in., active-matrix LCD screen is bigger and brighter than anything found on a laptop and, for many purposes, is superior to a standard monitor. Freed from concerns about battery life,



A MIGHTY SMALL PACKAGE

AKIA FUSION ONEBOX

- ▶ 14.5-in., active-matrix LCD display
- ▶ 233 Mhz Pentium II processor
- ▶ 32 MB RAM
- ▶ 4.3 GB disk hard drive
- ▶ Built-in Ethernet and 56-K modem
- ▶ \$2,999

AKIA AKIA CORP

which limit laptop design, desktop LCDs can offer brightness and contrast superior to cathode-ray tubes. LCDs are dead-flat and flicker-free. And their hard-edged pixels provide sharper images than the fuzzy dots on TV-

type designs. The biggest drawback: LCDs don't do very well with rapidly moving images, limiting their use with arcade-style games or full-motion video.

The Fusion gives a readable 1,024-by-768-pixel display. And while an LCD can't be viewed from as wide an angle as a CRT, the Fusion screen swivels vertically through an angle of more than 90 degrees, allowing for a wide range of seating positions.

The computer part of the Fusion outperforms any current Windows laptop. The base model includes a 233-megahertz Pentium II processor, 32 megabytes of memory, a CD-ROM drive, and a 4.3-gigabyte disk drive. For an extra \$400, you can upgrade the processor to 266 Mhz, double the RAM to 64 MB, and boost the disk capacity to 6.4 GB. The size of the chassis limits expansion capacity. The box includes a single slot for a PCI expansion card. Just about everything you might want in a business computer is already there, including an Ethernet connection, a 56-kilobit-per-second modem, and a sound system using small but adequate speakers.

Micro-PCs like the Fusion are popular in Japan, where desk space is at a great premium. Until recently, I wouldn't have given them a chance in markets outside of Asia. But I've reconsidered since the cost of flat-panel displays has dropped by at least half in the past year—even as their quality has equaled and surpassed CRTs.

As a result, I expect to see a profusion of flat displays, both in all-in-one units like Fusion and together with conventional PCs. The cost difference between a 14.5-in. LCD and a 17-in. monitor with a viewing area just a bit larger is down to about \$700. For an executive, that may not be a lot to pay to get that monster monitor off the desk.

HELP DESK



YEAR 2000

WHO'S READY?

Several readers responded to my Mar. 2 column on Year 2000 and PCs, asking how personal-finance programs handle the millennium. They do pretty well, but there are glitches, particularly with the market leader, Intuit's Quicken.

Current versions of the major personal-finance applications—Quicken, Microsoft Money, and MECA's Managing Your Money—can all handle dates starting in 2000 without difficulty. But the oldest editions of Quicken, versions 1 through 4 for DOS, will choke on dates after 1999.

All versions of Quicken for Windows have a problem with dates after 2027. Intuit says Quicken 6 and Quicken 98 will correctly handle 30-year bonds and mortgages whose maturity already extends past 2027 and that the problem will be eliminated in future versions. (Also see www.intuit.com/support/quicken/faqs/win/1345.html).

Microsoft says older versions of Money can handle dates until 2075, while Money 98 is good until 2200. MECA says all versions of Managing Your Money are compliant.

All of the programs assume that your computer has the current date set correctly. And the interpretation of an entry such as "2/5/05" varies by product and version. If in doubt when entering data, use four-digit years.

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Carole Pedriana, National Manager, New Era Business Project



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BY ROBERT J. BARRO

SO YOU WANT TO HIRE THE BEAUTIFUL. WELL, WHY NOT?



IT MATTERS:
A worker's
appearance
is as legitimate
a qualification
as intelligence
and experience
—so the
government
should butt out

In times past, stewardesses were often attractive women, which added to the pleasure of many heterosexual male air travelers. Gradually, since a 1971 lawsuit against Pan Am, however, stewardesses have become flight attendants, who are much less likely to be attractive and are sometimes male.

Many people view these changes as progress. Instead of pandering to the tastes of straight male customers, airlines now largely ignore such traits as sex, age, marital status, and appearance and focus instead on qualifications and seniority. Is it not a good thing if flight attendants are selected by job skills, meaning the ability to serve people well and to carry out safety procedures efficiently, and not at all on physical appearance?

I would say no. I believe the only meaningful measure of productivity is the amount a worker adds to customer satisfaction and to the happiness of co-workers. A worker's physical appearance, to the extent that it is valued by customers and co-workers, is as legitimate a job qualification as intelligence, dexterity, job experience, and personality.

Almost everyone can recognize that severing the link between wages and intelligence would reduce efficiency or lower the gross national product because brain power would not be allocated to its most productive uses. Yet outcomes based on intelligence are clearly unfair in the sense that, by and large, smarter people end up richer, and being smart is to a considerable extent a matter of luck. If one wanted the government to redistribute resources from smart to stupid people, then one would have to believe that the benefits from this redistribution would exceed the resulting losses in national product.

The same reasoning applies to physical appearance. This trait is highly valued in some fields, and reducing its importance to employment and wages would effectively throw away national product. The outcomes are also unfair, in the same sense as they are for intelligence. An interference with the market's valuation of physical appearance is justified only if the benefits from the redistribution of resources from more attractive to less attractive people are greater than the losses in overall product. Thus, it makes no sense to say that basing employment and wages on physical appearance is a form of discrimination, whereas basing them on intelligence is not. The two cases are fundamentally the same.

Most people (and the law) accept this approach to beauty for movie and television personalities and modeling. Obviously, there would be a great loss of national product if the government were to dictate that Cindy Crawford had to be replaced by me in all of her commercials. But the difference between glamour fields and others in terms of the role of physical appearance is merely a matter of degree. If the government stays out the market will generate a premium for beauty based on the values that customers and co-workers place on physical appearance in various fields. Probably the market will allocate more beauty to movies, television, and modeling than to assembly-line production and economic research. I have no idea how much beauty the unfettered market would allocate to flight-attendant jobs or CEO positions. But whatever the outcomes, are the judgments of government preferable to those of the marketplace?

Some solace can be taken from last fall's Hooter's settlement, which allows the restaurant chain to continue to limit its service staff to attractive young women. Physical appearance remains legally as a "bona fide occupational qualification" in this business. Of course economic reasoning would imply that physical appearance is always a bona fide worker characteristic as long as customers and co-workers think so.

UGLY STATS. Research studies, such as those by Daniel S. Hamermesh and Jeff E. Biddle in the 1994 *American Economic Review*, indicate that the wage differential between attractive and ugly people is about 10% for both sexes. The differential is substantially greater for women if one considers outcomes in the marriage market. Less attractive, or at least obese, women are much less likely to marry than non-obese women and tend to have husbands with sharply lower earnings. Some researchers have greeted these findings with regret.

To really address this hard fact of life, ugliness would have to be protected as a disability under the Americans with Disabilities Act, and the act would have to be extended to the marriage market. After all, what could be more unfair than the tendency of attractive people to obtain higher-earning mates? Perhaps a better idea than this new intervention would be for the government to stay out of the beauty business.

Robert J. Barro is a professor of economics at Harvard University and a senior fellow of the Hoover Institution.



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BY GENE KORETZ

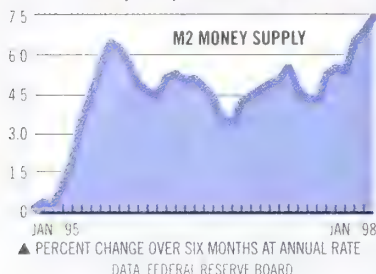
MESSAGE IN THE MONEY SUPPLY

The Fed may need to clamp down

In a widely reported speech in September, Federal Reserve Chairman Alan Greenspan pointedly noted that "inflation is fundamentally a monetary phenomenon." Small wonder, then, that many economists are casting a wary eye on the latest money-supply numbers.

Not only did M2 and M3, the most closely watched monetary aggregates,

MONETARY GROWTH: UP, UP, AND AWAY



exceed the target ranges set by the Fed last year, they have accelerated sharply in the past six months and are both rising at their fastest rates in the current expansion. At last count, M2 was growing at a 7.4% annual pace, while M3 was up at a heady 10.8% clip.

Meanwhile, Greenspan revealed in his recent Humphrey-Hawkins testimony before Congress that the Fed is maintaining last year's maximum growth targets of 5% and 6% for M2 and M3, respectively, in 1998. The fact that the Fed failed to nudge the targets higher suggests that policymakers regard the surging money supply with some concern. Although the Fed has downplayed money as a factor in its policy decisions on the grounds that the relationship between it and economic activity is uncertain, Greenspan's testimony noted that the relationship has recently "come back more into line with historical patterns" and was actually stable last year.

What is undeniable is that both monetary growth and economic growth exceeded the Fed's expectations last year and could well do so again in 1998. Economist Robert E. Mellman of J.P. Morgan & Co. points out that the Fed's quarterly survey of senior bank-loan officers last month not only showed no

tightening of lending standards but also indicated that loan demand is now rising on a broad front.

The bankers report that demand for home and commercial mortgages have accelerated sharply, business loans are continuing to rise, and even consumer installment loans are starting to strengthen. While foreign trade is weakening and business investment seems to be slowing, says Mellman, interest-rate-sensitive and credit-driven sectors are taking up the slack.

Like the Fed, Morgan economists tend to see such developments as an offset to a developing sharp economic blow from Asian turmoil. But the rapidity of monetary and credit growth, the upturns in housing, auto sales, and commercial real estate, and the still-buoyant stock market are leading some observers to wonder if domestic demand may prove too strong and the hit from Asia too weak to obviate the need for Fed tightening in the months ahead.

"It's not surprising," says Mellman, "that Greenspan's latest remarks have stressed the Fed's determination to hold the line on inflation."

A GOOD TIME TO BE A BIG WHEEL

Global demand for execs is way up

Despite turbulence in the global economy last year, worldwide demand for senior executives rose by a heady 18%, reports executive search firm Korn/Ferry International. The increase in hiring of execs earning \$100,000 or more was the largest since 1994. What's more, fourth-quarter results were unusually strong, a sign that business confidence regarding continued growth remains high.

Among the industries hiring, financial-services and industrial companies head the list in most regions. Other leaders included health services and pharmaceutical companies in North America, consumer-goods producers in Latin America, and technology companies in Asia. Although demand in Asia stayed firm last year, Korn/Ferry

sees a slowdown ahead—but, predictably not for mergers-and-acquisition specialists and workout experts.

ARE PROFITS LIFTING WAGES?

In key finance sectors, it seems so

One of the developments that has sparked inflation fears—and jolted the bond market—in recent weeks is the Labor Dept.'s report that the employment cost index (ECI) for private-sector workers surged by 1.2% in the fourth quarter, its largest quarterly rise in five years. On a year-over-year basis, private-sector compensation growth—which measures changes in both wage and benefits, accelerated to 3.4% from 3.1% at the end of 1996.

The big fear, of course, is that the pickup resulted from rising wage pressures in a tight labor market and will inevitably lead to higher prices as companies seek to protect profit margins. But economist James Glassman of Chase Securities Inc. argues that the wage surge reflects "strong productivity growth and robust profitability rather than an inflationary threat."

Virtually all of the fourth-quarter acceleration in private-sector compensation, and much of the 1997 rise, he notes, was accounted for by an unusual surge in the finance, insurance, and real estate sectors. Outside of those sectors there were crosscurrents, with wage slowdowns in manufacturing and trade offset by modest pickups in services and transportation.

Glassman points out that ECI wages and salaries include sales commissions earned by stockbrokers, real estate agents, mortgage brokers, and others. And booming activity in stock and real estate markets also bolstered regular salaries—as well as overtime premiums, insurance and savings benefits, nonproduction bonuses, and other fringes that are counted as benefits.

The key point, of course, is that rather than crimping profits, such compensation hikes actually reflect rising profitability. Indeed, pretax profit margins of financial corporations surged to 20% late last year from 15.3% at the end of 1996—despite more generous payouts to employees. The bottom line, says Glassman, is that "excessively tight labor markets aren't the only reason why wages might rise. In the new economy, it's often because profits and productivity are rising, too."

A TIGHT MARKET FOR TOP EXECs

INCREASE IN HIRING OF SENIOR EXECUTIVES 1996 TO 1997



SO FAR, THE ASIAN CRISIS IS MORE BOON THAN BANE

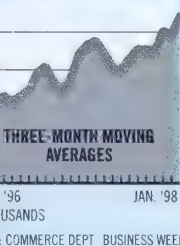
Consumers and homebuilders gain from lower rates and more buying power

U.S. ECONOMY

Is the Asian crisis actually helping the U.S. economy? If you laugh, look around. Lower interest rates are boosting housing and demand for home-related durable goods. Falling commodity prices, especially for oil, are cutting production costs. Cheaper imports are further curbing inflation, giving household buying power an additional lift at a time when wage growth is already slowing up. So where's the downside?

Be sure, plunging Asian output and its secondary effects around the globe will slow world growth in 1998. That will cut into U.S. exports, hurting mainly the manufacturing sector. However, keep in mind that the service sector produces half of U.S. output. It also employs three-fourths of private-sector workers, and it is largely immune to the Asian flu.

THE RISING TREND IN NEW-HOME SALES



Also, cheaper imports are bringing billions of dollars' worth of additional goods under the command of consumer budgets.

Still skeptical? Look at the latest data. In January, household real income rose strongly, and consumer spending was on a pace to rise at an annual rate of about 3.5% this quarter. Outlays for credit-sensitive goods are up, and in the past half-year, services have accounted for 80% of spending growth. Low rates and strong income growth will only reinforce these trends.

LOOK AT HOUSING, which is being pumped up by lower mortgage rates. Sales of new single-family homes soared in January, matching the 11-year high hit in November. Sales in the past three months are the highest since 1978 (chart), and construction outlays by homebuilders have surged in recent months amid low inventory, suggesting more gains to come. Moreover, with consumer spending and housing power fueling domestic demand, manufacturers appeared to be

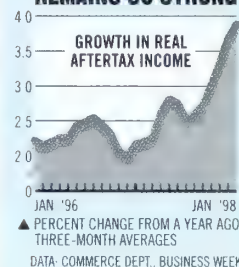
far from faring pretty well in February, at a time when Asian impacts should be hitting. The nation's purchasing managers say industrial activity remained sturdy last month, and while export orders fell, overall bookings were stronger for the second month in a row.

Consumer spending began 1998 with the same gusto that was evident in the second half of last year. Real outlays for goods and services, adjusted for inflation, rose 0.3% in January, only slightly below last year's robust second-half pace. Had it not been for a 6.1% drop in January outlays for electric and gas utilities, a result of unusually mild weather, real spending in the month would have increased an even stronger 0.5%.

Households shelled out mainly for two items in January, clothing and furniture, which accounted for nearly all of the month's gain in goods outlays. The jump in clothing purchases suggests that consumers took full advantage of post-Christmas sales, making up for sales declines in November and December—two times over. The jump in furniture buying shows that stronger housing demand is lifting sales of home-related goods, a trend that will continue in coming months.

The surge in outlays for services in recent months has been especially impressive. Real service purchases in January rose 0.2%, but the gain would have been twice that except for the drop in utilities spending. In the past year, overall consumer spending is up 3.1%, but service outlays, excluding utilities, are up 4.4%.

WHY CONSUMER SPENDING REMAINS SO STRONG



THE FOREMOST REASON

why consumer spending remains so strong is the vibrant pace of real after-tax income, which rose 0.7% in January, helped by a boost in government cost-of-living adjustments. But over the past year, real incomes have risen 4.1%, the strongest annual showing in three years (chart). Tight labor markets will keep incomes growing in coming months, and low inflation will assure gains in buying power.

Household spending will also get a lift as the benefits of past mortgage refinancings begin to kick in. Also, through Feb. 20, federal tax refunds were running 13.1% ahead of last year's pace, which will be putting even more money into consumers' hands.

Homebuilders undoubtedly are looking to the spring

building season with great expectations—and rightfully so. Their February assessment of market conditions was the highest in four years, and January's strong sales back that up. Builders may even be short on inventories, which could push up prices. In January, the supply of unsold new homes fell to a record-low 3.9 months, based on the current sales pace.

Homebuilding, which added solidly to fourth-quarter economic growth, will contribute even more this quarter. January construction outlays rose 0.7%, but excluding a drop in public-sector building, private-sector outlays jumped 1.2%, after a 1.1% gain in December. Housing led the advance, but business construction also rose in January, led by industrial building and office construction.

THE FEBRUARY REPORT from the National Association of Purchasing Management suggests that, despite weakness in the foreign sector, domestic demand is keeping industrial activity chugging along (chart). The NAPM's overall index rose to 53.3% last month, up from 52.4% in January. A reading greater than 50% means that the factory sector is growing. And in February, it grew at a bit faster pace than in January, as orders, production, and employment each picked up.

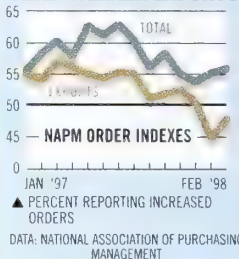
One possible stumbling block in coming months is inventories, which grew in the fourth quarter at a much faster rate—\$74 billion instead of \$59.9 billion—than the Commerce Dept. had initially reported in its first

estimate of fourth-quarter gross domestic product. Output of goods is starting to run ahead of goods demand, a situation that could lead to production cutbacks. However, inventory growth still does not appear to be excessive compared to demand.

Note that a key feature of the revision to fourth-quarter real GDP growth, from 4.3% to 3.9%, was that the \$14.1 billion upward revision to inventory growth was offset by a \$14.5 billion upward refiguring of imports. More imports widened the trade gap, causing lower GDP growth. However, those revisions suggest that imports accounted for much of the upward adjustment to inventory growth, not U.S. output. Higher stocks of foreign-made goods would tend to lessen the impact of any inventory adjustment on U.S. producers.

Clearly, the Asian crisis is far from a win-win situation for the U.S. economy. Many U.S. multinationals and exporters will end up net losers. But all the surprises so far have been on the plus side, which explains why the Dow Jones industrial average recently pushed through 8500. Perhaps the Dow's message is: Find something else to worry about.

ORDERS: STILL STRONG AMID WEAKER EXPORTS



ITALY

IT'S NOT JUST THE DEFICIT THAT NEEDS TAMING

Thanks to fiscal austerity and a stronger-than-expected economy, Italy reported on Feb. 27 that its public deficit had fallen below the target set by the Maastricht Treaty. Debt outstanding, however, remains twice the Maastricht target and will prove more intractable than the government deficit.

A healthy economic rebound helped the government of Prime Minister Romano Prodi pare the deficit from 6.7% of gross domestic product in 1996 to just 2.7% in 1997. Real gross domestic product grew 0.2% in the fourth quarter from the third, and 2.8% for all of 1997 (chart). Government incentives for car buying lifted consumer spending, but ex-

ports and inventory accumulation also boosted growth at yearend.

The expansion will continue this year. The Italian research institute Isco forecasts real GDP growth of 2.4% in 1998, with im-

proved domestic demand and further export strength. The first-quarter data look encouraging. The Confindustria survey showed that manufacturers expect that February output was up 0.5%, continuing the rebound started in 1997. Sales and orders were also expected to have risen. Meanwhile, inflation remains mild. Consumer prices rose 0.4% in February, and they are up 1.8% from a year ago.

The only sour note is a drop in

consumer optimism: Italy's confidence index slipped to 118.7 in February, from 120.8 in January. Households expect that the jobless rate, officially reported as a hefty 12.4% in the fourth quarter, will go higher. Even so, the confidence readings of the past two months remain above their fourth-quarter average.

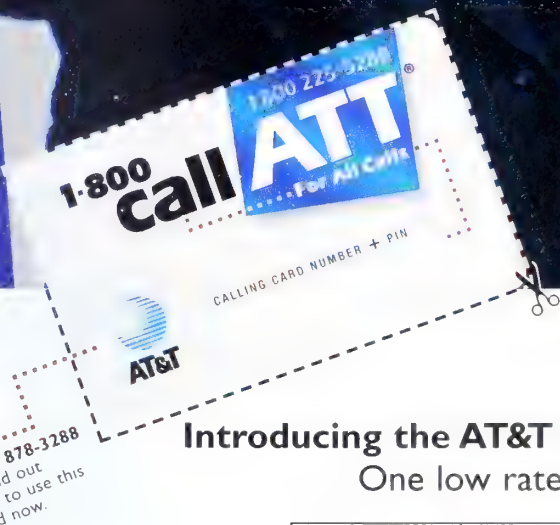
Prodi has promised "a coherent policy of rigor" for future fiscal decisions. But because of past profligacy, Italy's lingering problem will be its debt outstanding which totaled 121.6% of GDP in 1997. The Treasury Minister has said the ratio will fall to 100% in six years, but private analysts are skeptical. Still, Italy's claim as a founding participant in Europe's single currency is solid, and further cuts in interest rates, probably after its entry is ratified, are expected.

ITALY: WELL ON THE REBOUND ROAD



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AT&T

Bill Gates looked as if he'd prefer a pie in the face. There he was, the richest man in America, the ruler of cyberspace, trapped in a Capitol hearing room between windy low-tech senators and nasty high-tech rivals, including Sun Microsystems CEO Scott G. McNealy, who argued that Microsoft's market grip is on par with "General Motors having the ability to decide what type of gasoline you put into your car."

Officially, this bit of televised political theater—a Mar. 3 hearing of the Senate Judiciary Committee arranged by its chairman, Orrin G. Hatch—was mounted to explore just how competitive the software business is. But it also served

America Online CEO Stephen M. Case.

At the same time, politicians of every stripe see high tech in their future. House Speaker Newt Gingrich (R-Ga.) famously called for giving all poor Americans a laptop PC. And even before they took office, the Clintonites wooed Silicon Valley with promises to link Americans to the Information Superhighway. "The rapid growth in high-tech industries and globalization of the marketplace present new realities and challenges in every aspect of law and regulation," Vice-President Al Gore told *BUSINESS WEEK* in an interview on Mar. 3 (page 28).

True enough. The Internet and electronic commerce have been rearranging

James L. Barksdale and Michael S. Dell, CEO of Dell Computer Corp. On Feb. 25, Cypress Semiconductor CEO T.J. Rodgers and execs from Microsoft, Texas Instruments, and Sun urged the Senate Judiciary Committee to permit more visas for high-tech workers (page 30). On Mar. 4, another coalition began a campaign to lift export controls on encryption technology. And the entire industry is lobbying furiously for better global copyright and patent protection.

SHORT HONEYMOON? The industry's growing focus on Washington already has borne fruit. In the past few weeks, President Clinton pledged to keep the Internet tax-free for now, and Hewlett-Packard Co. won approval to export so-

SCOTT AND BILL WENT

High-tech leaders find that they can no longer afford to

to prove just how important the exploding high-tech industry has become to Washington policymakers, and vice-versa. "It's been a year since I was in D.C.," Gates wrote in his online zine *Slate* on the eve of the hearing. "I think I'm going to be making this trip a lot more frequently from now on."

Indeed he will. As the titans of high tech seize ever larger chunks of the global economy, an industry that a decade ago only dealt with government sporadically is now warily taking on the pols of the Potomac on dozens of issues. With growing debate in Washington over everything from computer privacy to antitrust, "it's increasingly clear the industry's future is less about technology and more about policy," says

the business landscape—changing how we buy everything from Buicks to books. Now, the leaders of the emerging digital economy are sweeping into the capital, changing the power relationships there, too. On the Internet, companies such as Microsoft Corp. and Netscape Communications Corp. are spreading into all sorts of digital services, from entertainment to online banking to telephony. As they do, they find their interests bumping up against the old guard that has played the Washington game for years—broadcasters, phone companies, even computer-hardware makers.

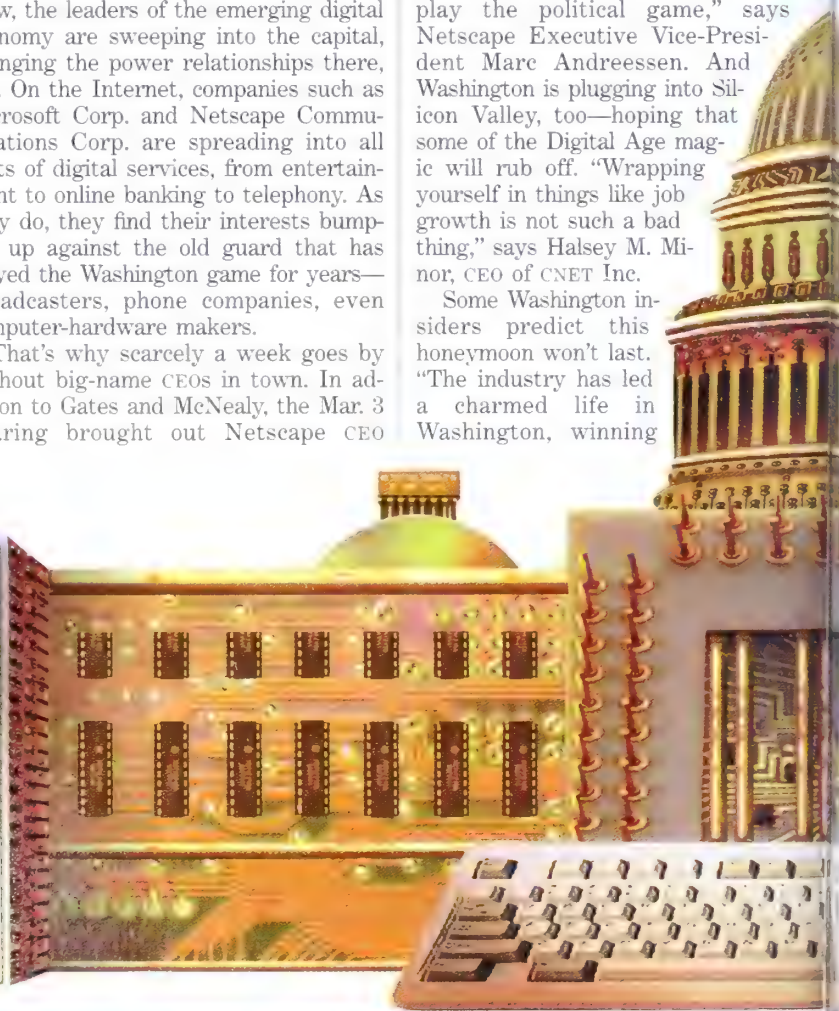
That's why scarcely a week goes by without big-name CEOs in town. In addition to Gates and McNealy, the Mar. 3 hearing brought out Netscape CEO

phisticated cryptography chips. The victories "show the Valley is learning to play the political game," says Netscape Executive Vice-President Marc Andreessen. And Washington is plugging into Silicon Valley, too—hoping that some of the Digital Age magic will rub off. "Wrapping yourself in things like job growth is not such a bad thing," says Halsey M. Minor, CEO of CNET Inc.

Some Washington insiders predict this honeymoon won't last. "The industry has led a charmed life in Washington, winning



SCOTT MCNEALY



after victory without having to
very hard," observes former Na-
Security Agency official and en-
on expert Stewart A. Baker. But
se the industry does not speak
one voice and because other in-
es are beginning to fight back as
ech companies encroach on their
Baker predicts trouble ahead:
y victory in Washington comes
he seeds of the next defeat."

ere's also potential for a huge cul-
lash. Gates's barely disguised dis-
or government is not anomalous.
industry had an attitude that gov-
ent should do what it needs to do
ave us alone," complains one Hill
ology staffer. "Their hands-off ap-

that directly addresses their own con-
cerns, assuming the wisdom of its argu-
ment would be hard to ignore.

To win the policy battles to come,
though, the new elite may need to learn
lobbying. Internet access providers, for
example, are likely to go head to head
with phone companies as the Federal
Communications Commission mulls con-
cepts such as Internet telephony. And
few lobbies in Washington can match
the power of the telcos. "These incum-
bent interests are not going to go gentle
into this good night," warns Kenneth
R. Kay, executive director of the Com-
puter Systems Policy Project, a group of
computer industry CEOs.

The clashes have already begun. Last

UP THE HILL

ore Washington—and vice versa

n to Washington will come back to
unt them." Admits Valley guru
Regis McKenna: "A lot of Silicon
Valley types still don't get it."

And when it comes to play-
ing the Washington money
game, many don't even try.

TechNet, a policy group or-
ganized by the super-con-
nected venture capitalist
John Doerr (page 29), is
an exception. To help ad-
vance the group's agen-
da, members have giv-
en between \$2 million
and \$4 million to both
parties. For the most
part, however, techies
favor issue advertising

year, computer companies fought tooth
and nail at the FCC to get a high-defini-
tion TV format that was compatible with
PC technology. In the end, they settled
for multiple standards—still impressive
headway vs. the awesome power of
broadcasters.

Of course, high-tech companies aren't
exactly novices. "It's a silly notion that
we haven't been here and we don't
know what we're doing," snorts Sun's
McNealy. His company set up its first
Washington policy office in 1992. IBM
has been here for decades.

High tech rode high during the Rea-
gan Administration. The Semiconductor
Industry Assn. mounted a huge crusade
to fight alleged Japanese dumping of
computer chips—repeatedly parading

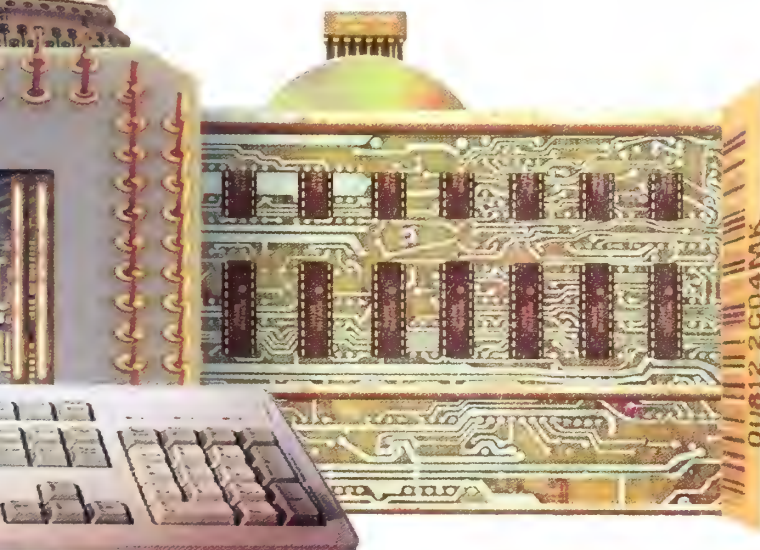
HATCH 2, GATES 1

So how well did Bill Gates do
on Capitol Hill? On balance,
not great. To be sure, Micro-
soft Corp.'s chairman held up under
fire—making his points about the
healthy state of innovation and
competition in software. But the
impression he left is that Microsoft
has enough market power in its
industry to justify further investi-
gation by federal trustbusters.

Again and again, Utah Senator
Orrin G. Hatch hammered away
with two questions: Do you deny
that Windows is a monopoly? Do
you prevent content providers from
promoting your competitors'
browsers? Despite carefully crafted
answers, Hatch drove home his
point. Gates acknowledged that just
days before the hearing, Microsoft
had dropped contract language that
prevented 40 leading Internet ser-
vice providers from promoting rival
browsers. And Gates's hand-picked
witness, Michael S. Dell, was
tripped up when Ohio Senator Mike
DeWine told him his staff couldn't
order a Netscape browser from Dell
because of its Microsoft contract.

The Senate Judiciary Committee
has no plans to seek changes in an-
titrust laws to make life more diffi-
cult for Gates. But Hatch's hearing
can only strengthen the Justice
Dept.'s resolve to prosecute Micro-
soft under existing laws. The score
so far: Hatch, 2; Gates, 1. Stay tuned.

By Steve Hamm in San Francisco



BILL GATES

such luminaries as Intel Corp.'s Bob Noyce before Congress. That led to the 1986 semiconductor trade agreement that stopped the dumping of Japanese chips in the U.S. and set market-share goals for U.S. chips in Japan.

LITTLE PATIENCE. But that success also led to a split in the high-tech community that diluted its influence. After the chip agreement led to DRAM shortages in the late 1980s, computer makers realized they needed a rival Washington presence. So they set up the Computer Sys-

tems Policy Project, one of many coalitions that sprouted up in the past decade. "The semiconductor guys ended up spawning us because we didn't like what they had done," recalls CSPP's Kay.

Now, the Internet era is bringing a new set of high-tech heavyweights into Washington policy circles. Unlike chip and computer makers—many of which benefitted mightily from government and defense contracts—these Internet and software tycoons have little patience for bureaucratic oversight and tend to

be uncompromising. The U.S., Gates warned at the Mar. 3 hearing, will only continue to lead in the Digital Age "if innovation is not restricted by government." That attitude rankles McKenna. "Bill Gates perfectly represents the techno-elitist view. He came out and said the government was full of B.S."

What do high-tech's new policy wonks want? While split on many issues—most notably how to deal with Microsoft's power—they agree on a few key points. One is easing immigration restrictions

A BOOSTER IN BLAIR HOUSE

Except for the occasions when Bill Gates is in town, there's no high-tech booster in Washington with a higher profile than Vice-President

Al Gore. The Veep, who is the Administration's point man on tech policy, not only wants to nurture the industry, he says he hopes to use its innovations to create a more efficient government. On Mar. 3, the Vice-President shared his views on technology with Washington Bureau Chief Lee Walczak, Senior Correspondent Howard Gleckman, and White House Correspondent Richard S. Dunham.

Q: This Administration presents itself as very much in sync with high tech. What does that mean in terms of policy?

A: It means listening and understanding the special needs that high-tech companies have. And then working in partnership with them. Just to pick one example out of many: There are 350,000 high-tech jobs that cannot be filled, partly because our educational and job-training institutions cannot produce the people with the skills to fill them. But there are many similar exam-

ples. And you don't know about them if you don't spend the time trying to understand this New Economy.

"It's really exciting to have all these entrepreneurs out there, all these dynamic CEOs"

AL GORE

Vice-President



stand how Washington works?

A: I saw a movie at the drive-in in Carthage, Tenn., when I was a little boy. It was called *Godzilla Meets Rodan*. They had different ways of relating, too.

Q: Have regulators learned to deal with high-tech enterprises?

A: Both the rapid growth in high-

Q: The industry wants to increase quotas for high-skilled immigrants. Why haven't you agreed?

A: We've made no decision on that issue. The Administration's first priority will be to ensure that American workers have the opportunity to acquire the skills they need to fill these jobs and have priority over any foreign workers with similar training. And to the extent we can accelerate dramatic improvements in higher education and job training to give Americans those skills, there will be less need for immigration waivers.

Q: Does the high-tech industry understand how Washington works?

technology industries and globalization of the marketplace present new realities and challenges in every aspect of law and regulation. But in our country, we find time and again that our oldest principles always apply to new situations.

I'm a fan of most high-tech companies. It's really exciting to have all these entrepreneurs out there, all these dynamic CEOs, all these employees coming up with new ideas and doing well by their families and communities at the same time that they are shaking the foundations of the world into which they were born. I'm thrilled by it.

Q: You are urging states to refrain from taxing Internet commerce. But in practice, don't such "infant industry" protections stay in place long after their useful life?

A: We're for a limited moratorium. We have agreed to support it only on the condition that the industry enter into a dialogue with state, county, and local governments on a solution that doesn't cause sudden infant death syndrome for the industry.

Q: Do you feel that the techies still have this Wild West, libertarian streak and want to be left alone by Washington?

A: I think it's both a cartoon-like distortion and a definite strain of thought within a significant portion of the industry. In government, there is always a two-way flow of ideas between the realm of public policy and the business world. These execs go through the process where they first want a place at the table and then decide: "Hey, it's our table too."

her is securities-litigation reform. on lost favor in the Valley in De- er, 1995, when he vetoed a bill that l have made it harder for share- rs to bring what the industry con- s frivolous lawsuits. "Clinton's veto ed high tech out of its relative qui- s," says Representative Tom Campbell (Calif.). "They'll never be passive." Silicon Valley mobilized, helped Congress to override the veto. And lowed up with a successful cam- gainst Prop. 211, which would shielded California shareholder suits the tougher federal restrictions. the moment, there's a rift be-

tween the software and Internet com- panies and the older computer makers over encryption. The government wants to limit exports of encryption technology to keep it out of the hands of terrorists. FBI Director Louis J. Freeh wants domestic restrictions, too. "The hardware guys, with all their ex- perience in Washington, are willing to look for compromise, whereas the nou- veau software guys want to have it all their way," says Kenneth Flamm, an economist at the Brookings Institution. Not surprisingly, hardware companies have gotten further. "Saying, 'Screw you, FBI and Defense Dept.' is not a

productive approach," observes Flamm.

Veterans of the Beltway predict that even the most arrogant and libertarian software execs will quickly learn to play the Washington game. They can't af- ford not to, considering the multitude of issues on the horizon. Battles over everything from privacy to intellectual property to electronic commerce will shape the economy of tomorrow. Wel- come to Washington, Mr. Gates.

By John Carey, with Howard Gleck- man, Catherine Yang, and Susan B. Garland in Washington and Steve Hamm and Andy Reinhardt in San Francisco

THE 'NEW ECONOMY' AND ITS BIGGEST FAN

Venture capitalist John Doerr is famous for launching Silicon Valley startups such as Netscape Communications Corp. These days, however, the Kleiner Perkins Caufeld & Byers partner spends a chunk of his time pushing public policy—in monthly meetings with Vice-President Gore and through Technology Network, a nonpartisan group of high-tech CEOs. TechNet's top buttons: improved public education and securities litigation reform. Doerr shared his views with BUSINESS WEEK correspondent Steve Flamm.

What made you jump into politics?

It wasn't so much political as it was public policy. That's increasingly important to technology companies and to citizens. Technology is a bigger part of the economy, and the kinds of things we want to do fall under a really important umbrella called the New Economy. And to build the New Economy, we can't do it in our garages all by ourselves.

What is TechNet's goal?

We picked two issues we focus on. One is education reform. The other is legal reform. And more broadly, we think we should be a meeting maker. We've had 100 meetings with elected officials of both political parties.

Your group has people of all political persuasions. How does that work?

It's everything from neo-Liberals to neo-Libertarians. We focus on a few issues and we only take positions with a two-thirds vote. There's broad agreement that we want to advance

the growth of the New Economy.

Q: What is the New Economy?

A: The old economy, you learn a skill.

The New Economy is lifelong learning. The old economy is concerned with security; the new is risk-taking. The New Economy is job creation; the old is job preservation. The old economy is capital equipment. In the new, it's intellectual property that matters. The old economy is about the status quo. The New Economy embraces speed and change. The old economy is top down and highly regulated, and tends to be a zero-sum game: You win, I

lose. The New Economy is distributed, and instead of being highly regulated we form public/private partnerships. If the old economy is zero sum, the New Economy is win-win.

Q: What has TechNet accomplished?

A: Several things. In our first month, we got 300 executives to stand up and call for national education standards in each state to measure if 8-year-old kids can read and 12-year-olds can do math. Last week, we pledged to fund and do



"If the old economy is zero sum, the New Economy is win-win"

JOHN DOERR

Venture capitalist

what we can do to pass a major charter school initiative in California. Also, Marc Andreessen of Netscape came up with the idea of the Education Dashboard—technology for linking parents, teachers, and students. One other thing: We joined with other organizations to get federal securities litigation reform passed so companies can use this safe harbor to tell their investors about an uncertain future.

Q: How could the government improve the climate for investment in high tech?

A: The first and most important

thing they could do would be to adopt uniform national standards for securities litigation reform. Step No. 2 would be more federal funding of basic research in universities. This is me talking, not Tech Net now. We need support in Congress. Netscape didn't happen just because Marc Andreessen was smart. There was federally funded research that led to the whole Web revolution. The third thing they can do is check their damned politics at the schoolhouse door and get serious about public education.

By Howard Gleckman

HIGH-TECH TALENT: DON'T BOLT THE GOLDEN DOOR

Perhaps she's named Irina—a brilliant computer engineer from Kiev. She wants to come to the U.S. and bring her dreams of developing the next breakthrough in communications software. But if she doesn't make it in the next few weeks, she probably will be turned away.

That's the sad result of bad immigration policy. In 1991, Congress set quotas that allow only 65,000 high-tech workers to enter the country annually. The cap was part of a larger scheme to stem the flow of immigrants, legal and illegal. But with American companies scrambling to find programmers, engineers, and other highly skilled workers in a tight labor market, business fears the 1998 quota could be filled by May.

ON THE CHEAP. The high-tech industry is working with Senator Spencer Abraham (R-Mich.) to raise the annual quota of these so-called H1-B visas to 90,000. But companies are getting a chilly response from the Clinton White House, which argues that U.S. employers are trying to get foreign workers on the cheap when they should be investing more money in educating and training the domestic workforce. "Companies shouldn't be able to say, 'We'll use immigration law as our way out,'" says White House economic policy coordinator Gene B. Sperling.

The debate over wages and education misses the main point: The U.S. shouldn't bar entry to skilled and creative people at all. At the same time, there's no question that U.S. businesses must support and generate efforts to raise the quality of math and science schooling to ensure a sufficient domestic crop of programmers and engineers in the future.

But such educational reform will take years. In the meantime, skilled immigrants who want to work in the U.S. should be welcomed with open arms. Top-notch workers, no matter



BRAIN GAIN Workers from abroad such as TI's Fang contribute hugely to U.S. output

what their nationality, stimulate an economy, creating wealth and improving living standards overall.

Indeed, the high-tech revolution now helping to fuel U.S. economic expansion might not have been so powerful without the drive and creativity of gifted immigrants. Everyone knows about Andrew S. Grove, the Hungarian who co-founded chip-making giant Intel Corp. But there are hundreds of others. Two of Sun Microsystems Inc.'s founding quartet were foreigners. At Cypress Semiconductor Corp., four of 10 vice-presidents are immigrants—from Britain, Germany, the Philippines, and Cuba. Says Cypress CEO T.J. Rodgers: "What would [the U.S.] look like if the computer chip had been created in Europe because of our lousy immigration policy?"

Many immigrants arrive as students. Alan Gatherer, branch manag-

er of wireless communications at Dallas-based Texas Instruments Inc., came from Scotland to study at Stanford University. Simon Fang, who now works on complex integrated circuits at TI, is originally from Taiwan. He also came to the U.S. to attend graduate school, and thanks to an H1-B visa, was able to stay.

WHIZ KIDS. The ivy path makes the current visa restrictions all the more perverse. Foreign students come to the U.S. to profit from the best graduate education in the world. Some take jobs here. But under H1-B visas, they must pack their bags six years later. Other countries get the benefit of these U.S.-trained engineers and scientists.

When these immigrants leave, the U.S. loses more than just their talents. An extraordinary number of their children achieve great success, too. Example: Of the 40 finalists in this year's prestigious Westinghouse Science Talent Search Award, 16 are either foreign-born or children of immigrants.

Critics say immigrants take jobs from native-born Americans. Maybe a few do. But artificial barriers won't protect U.S. jobs for long. If U.S.-based companies can't get the skilled workers they need at home, they will set up shop elsewhere—be it Dublin or Kiev. "We are disarming the economy of the United States if we don't allow skilled workers to come in," argues Dell Computer Corp. CEO Michael S. Dell.

That's why it is essential for the U.S. to nurture the best workforce in the world. It shouldn't matter whether these top-notch employees are born in New York or New Delhi. America, a nation of immigrants, should never turn its back on people who want to come here to work. They have too much to offer.

Gleckman covers economic trends from Washington.

MAKERS

GM MAKE J-TURN IN EUROPE?

Launching a new Astra, but more needs to be done

not a pretty picture. Since 1994, General Motors Corp. has been losing ground in Europe. Its market share is falling, and with no turnaround in sight, GM's European executives have been feuding openly. In 1997, GM lost its lead on the Continent for the first time since 1986—a dramatic change from the early 1990s, when Europe generated most of the company's auto profit. At the time, GM thought it had time to clean up its problems.

With Asia in the dumps, Latin America stumbling, and U.S. sales flattening, GM needs a European comeback *toute de suite*. Officially, GM executives deny rumors of a management shakeup, but sources close to the company say a housecleaning is imminent. Louis R. Hughes, the Zurich-based head of GM's international operations, tried unsuccessfully to unseat J. J. Herman, managing director of GM's German subsidiary, Adam Opel, in 1996. Hughes is now moving back to Opel in June to oversee GM's push in Russia and the rest of the former Soviet Union. He will be replaced by L. Cowger, currently head of manufacturing for GM Europe.

CLUBBING? GM brass hopes the new Astra will get GM Europe back on track. "It will be a turnaround year for us," says Hughes. But Cowger will be faced with an immediate challenge: completing the launch of a new version of the Astra, which introduced a new Astra is Opel's hope for beating archrival Volkswagen, which introduced a

new edition of the best-selling Golf six months ago. Because last-minute changes delayed Astra production by six months, it now has to be squeezed between the new Ford Motor Co. Escort and a new Ford Motor Co. Escort this fall. "GM is in an uphill battle to fight," says Lawrence Lawson, an analyst at Salomon

Smith Barney in London.

To make up for lost time, GM is launching three Astra models simultaneously. Car-makers typically begin building one body style to work out bugs. But GM's factory in Bochum, Germany is building five-door hatchbacks and station wagons concurrently. Analysts believe GM, which has had a reputation for poor quality in Europe, may be asking for trouble with the \$2.3 billion project. Cowger says staggering the start of the four factories that will build the Astra will prevent glitches.

Even a problem-free Astra won't give GM the quick turnaround it needs. The cost of the launch will hold down earnings in 1998, GM officials admit. Moreover, Opel has lacked the resources to counter VW's new-product offensive. Salomon figures GM's models have been on the market for an average of 4.8 years, vs. VW's 3.6. It may take steep price incentives to move GM's aging models. But even then, says Standard & Poor's DRI, the company will finish 1998 with

11.4% of the western European market, down from 13% in 1995. GM officials say they plan a 50% increase in new products in the next five to seven years.

Meanwhile, to regain its position as Europe's most efficient carmaker, GM has committed \$417 million to retool its aging plant in Rüsselsheim, Germany.

Opel officials are fighting for an additional \$167 million to raze the old plant and start from scratch. Opel recently signed an agreement with union workers that will allow GM to reduce the Rüsselsheim workforce by up to 5,000 people.

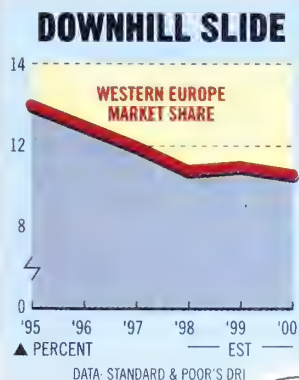
Even as GM builds up in Europe, it is scaling back its pell-mell rush into some Asian markets. A plant under construction in Thailand was cut from 80,000-unit capacity to 40,000, and the start of production there has been pushed back to mid-1999.

That mad rush into emerging markets sapped resources. GM Europe "is overextended, clearly," concedes G. Richard Wagoner Jr., president of GM's North American Operations. Now, Cowger will have to deal with internal as well as external problems to pull off a turnaround at Opel. Insiders say he has struck a conciliatory tone with workers. Hughes, who had hoped to follow Smith into the CEO job, will likely be under close watch by his Detroit colleagues. It may be years before GM regains its former strength in Europe—if it ever does.

By David Woodruff, with Kathleen Kerwin, in Geneva



HUGHES: GM's head of international operations vows: "This will be a turnaround year"



1998 OPEL ASTRAS

CORPORATE GOVERNANCE

GOVERNANCE DOC, HEAL THYSELF

CalPERS is under fire for its own potential conflicts of interest

Each year, as February draws to a close, directors at certain companies—they know who they are—cringe. That's when the California Public Employees' Retirement System (CalPERS) publishes its list of unresponsive boards. But this year, as publicists for the \$128 billion fund were blast-faxing the latest list, CalPERS found itself under scrutiny for the same kind of conflicts of interest that put corporations on its hit list.

After a recent series of *Los Angeles Times* stories alleging improprieties regarding CalPERS' \$3.3 billion fund for alternative investments, and one day after a state senator introduced legislation to place restrictions on California's public pension funds, the 13-member CalPERS board passed some new rules. The Feb. 19 reforms prohibit board members from taking campaign contributions from companies with current or potential business with CalPERS. And directors, who now are prohibited from accepting gifts worth more than \$290, must make a monthly report of gifts valued at more than \$50.

OUTSIDE MOVES. This effort, however, may not be enough. According to Democratic State Senator Adam Schiff, the Securities & Exchange Commission is investigating whether to restrict campaign contributions to directors of public-pension boards. And the FBI has made inquiries at California's two big public-pension funds. The SEC and FBI won't comment. CalPERS President William D. Crist says the fund has even the FBI public documents but says no probe has been started. The most vocal Cal-

PERS critic has been Schiff, chairman of the California Senate's public employment and retirement committee. His concern was sparked by a \$100 million investment in a Hicks, Muse, Tate & Furst Inc. leveraged-buyout fund that had hired a former CalPERS board member. The decision to invest in the fund was made despite strong objections over fees by CalPERS' staff. Hicks Muse CEO Tom Hicks disagrees with that judgment. Schiff also says the CalPERS board approved investing in a real estate venture partly owned by a board member's son-in-law. Crist says board members with conflicts abstain from voting.

Calpers also has in-house critics. State Controller and trustee Kathleen Connell questions the ethics of a 10-day trip to Asia taken in 1996 by several board members. The trip was paid for by a non-profit group financed by money-management firms that also sent representatives. A month before, CalPERS had approved a \$225 million investment in a fund run by one of those firms, San Francisco-based Lombard Investments. Moreover, Lombard officers, associates, and their families have contributed more than \$30,000 to the campaigns of GOP State Treasurer and board member Matt Fong, who organized the trip. Fong, now seeking a senate seat, says his contributors are on file at the Secretary of State's office and says he votes strictly on investment merits. And Crist defends the trip as educational. "I wasn't told who paid for anything, and I didn't ask," he says.

NOT THE FULL MONTY. Under the senate bill, any company trying to do business with California's big pension funds would have to disclose ties to board members or



FONG: Organized a China trip subsidized by a firm whose fund CalPERS invested in

gifts or political contributions to them. The bill would also limit communication between trustees and companies while the board is mulling proposals. And it would make board meetings more open to the public and mandate release of meeting transcripts within a year. So far, the reforms most directly affect the two state-elected officials on CalPERS board, Fong and Connell. Fumes Connell: "This doesn't go the full monty."

Both Connell and Fong, who call the recent measures "window-dressing," are pushing for greater disclosure. The CalPERS board plans to review its rules on trustee travel in March. Whatever the directors decide, it's clear that this corporate watchdog is likely to find itself on a shorter leash.

By Kathleen Morris
in Los Angeles

EXAMINING CalPERS' BOARD OF DIRECTORS

WHAT'S BEING QUESTIONED

- ▶ Members accepted free travel, meals, and gifts from contractors soliciting investment
- ▶ Members received hundreds of thousands of dollars in campaign donations from the investment industry
- ▶ Many CalPERS investment decisions have been made behind closed doors

THE NEW RULES

- ▶ Members can no longer accept campaign contributions from contractors or potential contractors
- ▶ Members must turn in a monthly report of all gifts worth more than \$50
- ▶ Transcripts of closed-door meetings must be released within 12 months

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COMMENTARY

By Wendy Zellner

HOW NORTHWEST GIVES COMPETITION A BAD NAME

With the Justice and Transportation Depts. scouring the airline business for predatory behavior, the big carriers are already screaming about "re-regulation." Indeed, in mid-March DOT is due to unveil controversial new guidelines on what constitutes anti-competitive behavior and the remedies DOT might demand.

Despite the airlines' protests, regulators have good reason to take a hard look at competitive tactics. And if they want a quick lesson, they could hop a flight to the Detroit Metropolitan Wayne County Airport. It's as good a place as any to learn how a dominant carrier can head off upstart rivals.

At Metro, Northwest Airlines commands 73% of the traffic, and new competitors say its behavior there strengthens their case that such "fortress hubs" can be immensely anti-competitive. Northwest spokesman Jon M. Austin says the nation's fourth-largest airline—now seeking approval to take a controlling stake in No. 5 Continental Airlines Inc.—is competing "fairly but aggressively." **"BLOOD IN THE WATER."** Upstarts like Spirit Airlines and Reno Air Inc. would beg to differ. Spirit tiptoed into the Detroit-Philadelphia market in December, 1995, with one round-trip flight a day, says Vice-Chairman Mark S. Kahan. Northwest's average one-way fare when the tiny Spirit entered was more than \$170. Spirit's introductory unrestricted fare: \$49 one way. For a time, the strategy seemed to work. For the most part, Northwest ignored tiny Spirit, which filled its 117-seat plane and made a profit, claims Kahan.

But after the May, 1996, ValuJet crash led to a drop in bookings for other discount carriers, Northwest "saw blood in the water," says Kahan. On June 30, 1996, Northwest slashed its fares to Philadelphia to \$49 on vir-

tually all seats at all times, he says. And it poured on capacity, adding nearly 30% more seats. On Sept. 30, Spirit abandoned the route. Says Northwest's Austin: "We're being criticized for matching a competitor's action, which I view as pro-consumer."

Executives at many big airlines say cutting fares and adding capacity is good for consumers. True, but only

ated by announcing daily nonstop service. When Reno said in March, 1997, that it would offer two flights a day, Northwest jumped to three daily flights. Northwest also undercut many Reno fares, the small airline contends, pricing "below an appropriate measure of its cost in providing such service," according to court documents. On Sept. 15, Reno cut back to one flight a day to Northwest's two. Northwest denies any wrongdoing.

Even two-plane Pro Air Inc., which flies from Detroit City Airport, about 25 miles from Metro, hasn't escaped Northwest's notice. Northwest dropped its fee for changing tickets from \$75 to \$25—matching Pro Air's—but only in the markets where it competes with the startup, says Pro Air President Craig E. Belmondo. And, he claims,

Northwest is offering 20% commissions to travel agents in Pro Air's markets, vs. the typical 8% elsewhere. "There is no doubt that Northwest does not want competition in this market," says Belmondo.

The startups in Detroit are hoping that the mere threat of litigation and a government crackdown will deter their big rival. But they're not counting on it. Indeed, small airlines nationwide feel seriously threatened by their larger rivals' practices. Economist Alfred E. Kahn, one of the fathers of airline deregulation 20 years ago, says rising prices and aggressive tactics could backfire for the big carriers. "The behavior of unrestricted fares in the last couple of years has been outrageous," he says. "It's not even in the interest of the carriers themselves to create such hostility and resentment." Sure, distinguishing between hard-nosed competition and outright predation won't be easy. But that doesn't mean the regulators shouldn't try.



if it lasts. By the first quarter of '97—just a few months after Spirit withdrew—Northwest's average one-way fare on the route had climbed to more than \$230, says Kahan. And the number of seats available from Northwest on the Detroit-Philadelphia run dropped, too.

Reno Air describes similar Northwest tactics in an antitrust suit filed in federal court in Nevada last March. Reno alleges that when it announced nonstop service in December, 1996, from Reno to Detroit—which Northwest had never served on a nonstop basis—Northwest immediately retali-

Its tactics in Detroit show how dominant players can drive out rivals and keep airfares high

Zellner is BUSINESS WEEK's Dallas bureau chief.

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CHAINS AW AL GOES TO CAMP

Sunbeam's chief will try to halt outfitter Coleman's slide

Hours after Sunbeam Corp. Chief Executive Albert J. Dunlap unveiled his planned \$2.5 billion trio of acquisitions on Mar. 2, the CEO of Coleman Co., the largest of the targets, jetted from New York to Wichita to comfort his troops. After all, Dunlap is famously intolerant of underperformers—and Coleman has been anything but stellar. Coleman CEO Jerry W. Levin, who is based in the Heartland. "We all feel bad we didn't get to play out our hand," he says. "But at the price we were offered, it was a great deal for shareholders."

True, at 35% on Mar. 4, Coleman's stock is more than double its yearend price of 16%. But the deal may not be so great for the 90% of Coleman employees without stock options. In a Mar. 2 conference call, Dunlap told analysts that the companies he is buying—Coleman, First Alert, and Signature Brands—"are not very different from the old Sunbeam or other companies I've done." Dunlap's prescription for Sunbeam included closing 18 factories, halving head count, and slashing product lines—lending further credence to his nickname, "Chainsaw Al." So employees may be right to worry about his plans for Coleman.

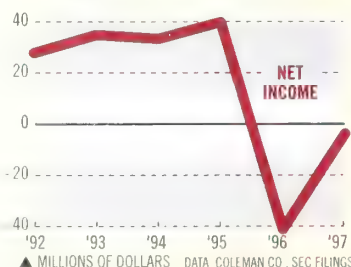
WEAK YIELD. How did Coleman come to this pass? It owns some of the top brand names in outdoor recreation in the U.S. and Japan—including Eastpak backpacks and Coleman itself. But it has not lived up to the potential those names afford. Indeed, Coleman, 83% owned by Ronald O. Perelman's MacAndrews & Forbes Holdings Inc., has been an unspectacular part of the mega-investor's portfolio. Perelman bought Coleman in 1989 for \$545 million. Until the sale, it accounted for a chunk of the debt on his books.

Allowing for the Coleman debt, Kevin M. Kuzio, an analyst with KDP Investment Advisors in Montpelier, Vt., estimates Perelman made \$814 million on the Mar. 2 deal. That would be just \$269 million more than he invested initially. A Perelman spokesman says that "our profits were well in excess of \$1 billion" if the proceeds from Coleman asset sales and spin-offs are included.

However you crunch the numbers, it's clear that Coleman has been running into



COLEMAN: DIMMING LIGHTS



trouble, posting losses for the past two years. Retailers and rivals say the company jumped the track under CEO Michael Hammes, who took the Coleman name downmarket with a proliferation of backpacks, coolers, lanterns, and tents sold through mass market retailers. "They seem to have gone completely for the white-trash market," says Michael Fowler, vice-president for operations at Uncle Dan's, a Chicago-area camping retailer. Fowler complains that quality has slipped, so he now limits his purchases to stoves, lanterns, and cheap accessories.

Then there were problems overseas. Coleman has strong distribution in Europe and Asia, but its sales there stalled in 1997. Indeed, to reduce inventory backlog, it didn't ship anything new to Japan during the second quarter, usually its strongest. Coleman added market

"They seem to have gone completely for the white-trash market"

MICHAEL FOWLER

Chicago camping retailer Uncle Dan's

share in Europe with its 1996 purchase of Germany's Camping Gaz. But the deal drove its debt levels over \$400 million, with little earnings payoff. Coleman was also hurt by troubles in Asia, once its fastest-growing market.

To try to repair the damage, Perelman dumped top management at Coleman, sending Levin, a longtime lieutenant, back to be chief executive after a term at the helm of Revlon. Levin cut 1,000 workers, closed four plants, eliminated a third of Coleman's products, and began selling off units to pay down debt. Losses in 1997 were trimmed to \$2.5 million, and margins rose 8%. But then along came Dunlap's offer, giving Perelman an exit.

And now? Dunlap is setting aggressive margin targets of 20%—far above Coleman's historic high of 13.4%. That will probably mean additional cuts in Coleman's product line. And, Levin says, Sunbeam may move some of its manufacturing to Coleman's Wichita plant and close more of Sunbeam's facilities. "They are going to do things we couldn't do on our own," he says. Sunbeam also expects to use Coleman's overseas distribution channels for its wares.

Dunlap is out to prove that Coleman can be a useful tool in his rucksack as he builds a global consumer-products company. That's probably bad news for many Coleman workers.

By DeAnn Weimer in Chicago, with Gail DeGeorge in Miami and Leah Nathans Spiro in New York



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TO THE INTERNET,
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"WHO CONNECTS
THEM TO THE
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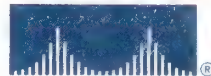
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COMMENTARY

By Mark Clifford

MURDOCH: PENNY-WISE, POUND-FOOLISH IN ASIA

Say this for Rupert Murdoch: He's not afraid to cower. The Australian media mogul has spent the past five years in China backing off from his famous 1993 statement that satellite television is "an unambiguous threat to totalitarian regimes everywhere." Four years ago he pulled BBC News off StarTV's China broadcast to protect his \$825 million investment in the satellite channel. Then he sold his stake in the *South China Morning Post*, one of the world's most lucrative papers, to avoid conflict with Beijing. Murdoch even published and hyped the anodyne memoirs of former paramount leader Deng Xiaoping's daughter.

So it's true to form that he would walk away from publishing the controversial memoirs of former Hong Kong Governor Chris Patten—whom Chinese officials branded a "strutting prostitute" for his advocacy of democracy in Hong Kong. "Business and politics and culture are interwoven," says Bruce Dover, News Corp.'s head of China operations. "That's the lesson we've learned in China."

So was News Corp.'s cravenness a smart business move? True, it's ahead of the competition in China. It has a joint Internet service with the *People's Daily* and a venture with the Tianjin People's Committee to operate a video production facility. Its part-owned Chinese-language channel now runs on cable—a first for a foreign



BEIJING: Murdoch is ahead of rivals, but StarTV has yet to turn a profit

the mess roiling Asia is that punishing truth-tellers means that the problems have more time to fester.

Asia is filled with examples where it would have been best to thank bearers of bad news rather than attack them. In Thailand, Goldman Sachs (Asia) Ltd. was called on the carpet in early 1997 for suggesting that the baht's peg to the U.S. dollar wouldn't hold. Goldman was right, but the central bank squandered billions in reserves defending the baht. Thai police even raided the Bangkok office of ABN Amro Asia Ltd. last year to check out whether the Dutch investment bank was encouraging investors to sell the Thai currency.

Korea First Bank went bust. The securities firm doesn't want to be identified because its report is the subject of a parliamentary investigation.

If there's any good news, it's that Asia's troubles make it more likely that honesty will be tolerated, if not encouraged. Look at Morgan Stanley, Dean Witter, Discover & Co. Chinese officials have cold-shouldered the firm since strategist Barton Biggs advised investors to sell the Hong Kong market during last October's meltdown. Biggs and the U.S. investment bank were criticized by the financial elite, and insiders say that Chinese President Jiang Zemin and Vice-Premier Minister Zhu Rongji were livid. Even now, officials still urge Biggs's firing.

Yet Morgan Stanley soldiers on, and execs say the controversy hasn't cost it business. It just headed up a \$150 million bond issue for Shanghai Industrial Holdings Ltd., one of the largest Chinese state companies listed on the Hong Kong exchange. "The American houses are pretty immune because people need American capital," says a Hong Kong-based executive at a European investment bank.

The lesson isn't that honesty pays. But it should. As Asia's financial crisis grinds on, leaders are likely to find that punishing bearers of bad news will carry an increasingly high price.

Clifford covers Asia for BUSINESS WEEK in Hong Kong.

THE PAYOFF News Corp.'s cravenness in its China dealings certainly won't help Asia—and it probably won't help Murdoch

satellite feed. But Murdoch might have done better—financially—to hold on to the *South China Morning Post*. Neither StarTV nor his other China ventures have ever turned a profit.

In the short run, it's often a losing battle for companies to stand up to Beijing, as Murdoch and others have found. But in the long run, it's not likely to help China or the beaten-down economies of Asia if honest debate is stifled. Indeed, one lesson of

In Korea, too, more openness would have saved tens of billions of dollars. Executives at a leading British securities firm were forced to apologize to officials at Korea First Bank in early 1997 after one of the firm's analysts warned about its loans to ailing Hanbo group. Immediately after a senior executive with the securities firm went on bended knee to Korea First, Hanbo group collapsed under its \$6 billion debt. In its wake,



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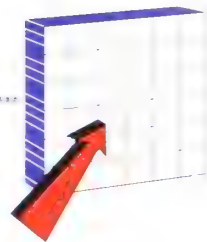
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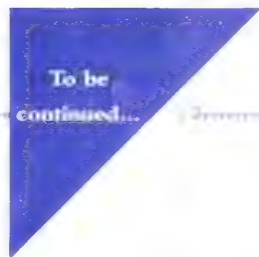


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EDITED BY PAT WECHSLER

UPS: WE ALSO CYBER-DELIVER

PACKAGE DELIVERY GIANT UPS is learning to love the Net. On Mar. 4, UPS announced a new service that will zip documents via the Internet in seconds rather than rely on planes, trains, and delivery trucks. Software from Tumbleweed Software and NetDox will ensure that delivery will be secure—unlike E-mail and attachments sent over the Web—when the service goes live in the second quarter, UPS says. The price: \$1 to \$10, well below UPS's basic \$12 document delivery fee. Analysts think 30% of documents will be cyber-delivered by 2000—a shift that would throw the \$8 billion

document delivery business into decline and give UPS a leg up against industry giant Federal Express. Meanwhile, the U.S. Postal Service is working on a similar secure E-mail service but has no start date scheduled.

WORLDCOM GETS SNAGGED ON THE NET

BUSY SIGNALS IN BRUSSELS? As WorldCom tries to complete its acquisition of MCI Communications, the European Union is voicing some objections over the two companies' combined share of the Internet market. The EU's antitrust enforcement arm says its review may take another four months. The objections are unlikely to stop the acquisition, but the EU could force certain conditions, such as guarantees that its Net backbone will be accessible to others. It also could force the combined company to divest itself of some Net businesses.

CLOSING BELL

PC OVERLOAD

Is Compaq suffering from indigestion? Shares of the industry darling stalled this year as unsold PCs piled up in dealer warehouses. Now, Wall Street expects the overhang to hurt Compaq profit margins and sales for the quarter ending Apr. 4. Compaq shares are down 19% over the past month. Meanwhile, shares of direct sellers, which don't worry about dealer inventory, have soared: Dell has climbed 29%, and even Apple, which plans to sell direct to consumers, is up 34%.



ADP GIVES TREES A BREAK

AUTOMATIC DATA PROCESSING, which distributes some 100 million pieces of annual-meeting material for corporations each year, is rolling out a system for distributing proxy material via the Internet as well as allowing shareholders to vote online. It expects that the system will be used at as many as 5,000 annual meetings this proxy season. ADP predicts that if it can convert even 5% of its annual-meetings mailings to cheaper online delivery, it could save as much as \$25 million.

THE MONEY STORE'S NEW MONEYBAGS

THE MONEY STORE IS THE latest trophy for the acquisitive Ed Crutchfield, CEO of

HEADLINER: MARC ANDREESSEN

NERVOUS AND SHAKY AT NETSCAPE?

A CASE OF POOR TIMING: Netscape Communications co-founder Marc Andreessen registered to sell 25% of his stock (375,000 shares) on the heels of the company's \$88 million fourth-quarter loss.

Is he losing faith? Andreessen says no. "My confidence in Netscape has never been higher," he says. So why sell? It's just time to diversify, he says. "I can't have all my wealth in Netscape."

What's worse, Netscape General Counsel Roberta Katz and Executive Vice-President Mike Homer are also unloading shares.



Katz's sale was prompted by her move to the San Francisco area from Seattle and the purchase of a new home. "This is an ever greater commitment to Netscape," she says. For Homer, selling 100,000 shares is part of a quarterly diversification gambit.

Still, Netscape's stock is trading at about 20—less than a quarter of its high—making this an odd time to sell. Says analyst Robert Gabele at insider-trading tracker CDA/Investnet: "This shows a lack of confidence in the future."

By Steve Hamm in San Mateo, Calif.

First Union. After snapping up two big banks and a brokerage firm last year, Crutchfield is plunking down \$2.1 billion in First Union stock, outbidding still undisclosed rivals to buy the Money Store, a company specializing in home-equity, student, and Small Business Administration loans. The consumer-finance industry has come under pressure as savvy consumers seek out low-cost credit, but First Union officials believe both the bank and the Money Store will benefit from gaining access to each other's customer lists.

TEXAS INSTRUMENTS DISCARDS ACER

TEXAS INSTRUMENTS IS TAKING another big step away from the DRAM business with an agreement to sell its one-third share of Taiwanese memory-chip venture, TI-Acer. Acer, TI's partner, which

is buying TI's share, already owned 49% of the operation, which reported pretax losses last year of \$143 million. Losing TI is no loss for Acer, though. Under the decade-long venture, TI was the chip fab's sole customer, forcing TI-Acer to sell all its chips to the U.S. company at a discount. Acer is renaming the company Acer Semiconductor Manufacturing and will diversify into other products, such as logic chips.

ET CETERA...

- Intel's first-quarter revenue will come in 10% below expectations.
- GM sales in February fell 7%, vs. a drop of 0.6% for Ford and a gain of 3.1% for Chrysler.
- The U.S. Supreme Court ruled to permit same-sex sexual harassment suits.
- Disney's second-quarter earnings will be off because of bad films and bad weather.

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ED BY OWEN ULLMANN

CORNERED CREDIT UNIONS COME OUT FIGHTING

The stiff setback that the U.S. Supreme Court handed credit unions on Feb. 25 may momentarily shackle their growth, but it has hardly stopped them in their tracks: They're mad as hell, and they're taking their case to Congress. Their goal is to convince lawmakers that in this age of personal megabanks, lending cooperatives are today's neighbors.

George Baileys. They may just pull it off. But first they're in for a nasty fight with the banks, which hope to unmask many of them as interstate combines posing as warm and fuzzy co-ops.

Under the high court's decision, member-based credit unions will probably have to stop signing up customers who are not employees. The case was based on the AT&T credit union in Winston-Salem, N.C.; two-thirds of its 165,000 members have no employee ties to AT&T. And there are more than a hundred big credit unions like that. The lure: Credit unions are tax exempt, so they can offer loans at lower rates than banks. The original intent was to provide credit for blue-collar workers unfed for bank loans, but these days a group of pilots to pro basketball players has its own credit union. The banks work that their rivals have used this tax advantage to grow membership to 73 million, with \$360 billion in assets.

WATCH? While the banking industry is footing the bill for the battle, it's community banks that are out front. They want Congress to revoke the tax-exempt status of the big credit unions and subject them to the same regulatory oversight as other lenders. "For many community banks, this is a life-or-death issue," says banking consultant Bert Ely. At first glance, it looks like a mismatch. The banking industry is a powerful force on Capitol Hill, with close ties to congressional leaders. It forked over \$13 million in campaign donations for 1996—or 17 times what the credit unions

gave. Besides, the Credit Union National Assn. (CUNA) was a sleepy trade group based in Madison, Wis., until it moved to Washington in 1996. "It's a David-and-Goliath situation," says ex-Representative Daniel Mica of Florida, who heads CUNA.

Although it lacks a strong Washington presence, CUNA has unleashed a grassroots blitz. Last month, 4,000 credit-union officials swarmed over the Hill with petitions signed by 2.5 million members. "There are a lot of congressmen who are going to have to compare PAC contributions against grassroots votes," says Mica. It wasn't hard to find sympathetic members: Representative Christopher B. Cannon (R-Utah) recalls how his university credit union "gave me the downpayment to buy my first house."



TREASURED IMAGE: George Bailey

He has introduced a bill to prevent credit unions from losing members because of the court decision. Another, sponsored by Representative Steven C. LaTourette (R-Ohio) and Paul E. Kanjorski (D-Pa.), would nullify the ruling. It's backed by more than 170 legislators, including Speaker Newt Gingrich (R-Ga.) and Senate Banking Committee Chairman Alfonse M. D'Amato (R-N.Y.).

Hill watchers expect the banks to resort to guerrilla tactics by focusing on the Senate, where a single member can block legislation. The banks are also counting on House Banking Committee Chairman James A. Leach (R-Iowa). He has vowed to attach the LaTourette-Kanjorski bill to a broad financial-services reform measure with scant progress for passage. It would be a "kiss of death" for the credit-union initiative, says a bank lobbyist.

That's probably wishful thinking. "I don't think 70 million credit-union members are going to be very forgiving if we don't have this issue straightened out by the time we go home this fall," warns LaTourette. With support like that, credit unions may find that it's still a wonderful life.

By Dean Foust

CAPITAL WRAPUP

SS CROWDED FIELD?

The GOP Presidential field for 2000 may be narrowing sooner than expected. After '96 Vice-Presidential nominee Jack F. Kemp gave a rambling, off-the-cuff speech at the Feb. 26-Mar. 1 Southern Republican Leadership Conference in Biloxi, Miss., party activists speculated that he won't even enter the race. Former Vice-President Dan Quayle also bombed with an unfocused press. Quayle didn't help erase his fee-prone image when he mispronounced "Slovenia."

GOP: GLAD GLENN'S GOING

► Senate Republican leaders can't wait for Senator John Glenn (D-Ohio) to return to space this fall. The retiring former astronaut, the ranking Democrat on the Governmental Affairs Committee, was surprisingly partisan during the panel's hearings on '96 campaign fund-raising abuses. Republicans prefer dealing with Glenn's likely successor on the panel: Joseph I. Lieberman of Connecticut. Lieberman is considered far less partisan and more moderate philosophically.

NET FUNDING BRAWL

► Federal plans to give schools and libraries discounted Internet service are hitting new snags in the Senate. Republicans and Democrats from farm states, including Appropriations Committee Chairman Ted Stevens (R-Alaska), fear the low-cost program will eat into another subsidy to hold down local phone rates in remote rural areas. The lawmakers, worried that the Net subsidy could cost more than \$2 billion a year, are mulling legislation that would shrink the funding.

CAN CHINA



Cover Story

VERT CRISIS?



WOLF AT THE DOOR Laid-off factory workers seek jobs in the northern Rust Belt

The swank bars and restaurants of Shanghai are filled with nervous talk these days about how the bottom is falling out of the local real estate market. Shanghai's five-year construction binge soaked up \$18 billion and astounded the world with its audacity. But now the city touted as the financial capital of the world's next superpower is filled with half-empty office towers and the concrete shells of apartment buildings. It may be Asia's biggest property glut yet.

Hundreds of miles away, in an export zone of the Pearl River Delta, the general manager of an import-export firm in Guangdong is worried, too. His company has been a star exporter of shoes and textiles. But now his suppliers are laying off half their workers, unable to compete with rivals in Southeast Asia who lowered prices after their currencies tumbled. With earnings dropping, this manager thinks he may have to cut workers, too.

China's economy is starting to sputter as the big sources of its economic strength all show signs of fatigue. Foreign investment is slowing because cash-starved Asian companies can no longer afford to build in China. Exporters are seeing business shift to cheaper factories in Thailand and Malaysia. The real estate boom in the rich coastal provinces is turning into a bust. Unemployment is rising, and bad loans keep piling up in the state-owned banks, threatening the health of the entire economy. True, China does not have the convertible currency and massive short-term foreign debt that triggered the meltdowns across Asia. But there are enough similarities that the outside world is now asking if China can avert a crisis.

Acutely aware that the country must change course, Beijing's mandarins are scrambling for solutions. As thousands of delegates meet in Beijing for the National People's Congress, the Chinese are waiting eagerly for signs of decisive action from new Premier and economics czar Zhu Rongji. "We need a New Deal with Chinese characteristics," says Chinese Academy of Sciences researcher Hu Angang, recalling the



Austerity programs are on the way out. Envisioned is a massive public-works program

bold economic activism of the U.S. six decades ago.

The pieces of China's new deal are still taking shape as the country's best and brightest pen white papers by the score. Much hinges on the outcome of leadership changes and a major shakeup of government ministries now under consideration. But some key elements are emerging: Instead of devaluing its currency to boost exports, the government will try a major policy shift. To stimulate domestic growth it will abandon its current austerity program and promote hundreds of billions of dollars in new investment over the several years, much of it in public works and housing. The government will likely raise most of these funds by significantly expanding its fledgling bond market and loosening up on credit. And Beijing will inject \$32 billion in fresh capital into the country's four top banks so they can start shedding bad loans.

TWIN OBSESSIONS. For Zhu Rongji, who is expected to take over as China's Premier at the Congress, the moves to prime the pump signal a big change in thinking. Through administrative fiat, Zhu—nicknamed *Lao Ban*, or The Boss—started to choke off credit in mid-1993 to squeeze out speculation in the property and stock markets. His other obsession has been stopping inflation, which has cooled from 22% in 1994 to under 1% now. Associates say Zhu ignored

CHINA: THE PROBLEMS

BANKS The government channeled 75% of bank credit into state enterprises. But this practice has produced at least \$240 billion in bad debt and created a bank insolvency crisis.

EXPORT SLOWDOWN Coastal provinces absorbed billions in foreign investment to build factories for overseas markets. But Asia, which accounts for half of exports, has collapsed, and foreign investment has slowed.

SPECULATION Billions have poured into office buildings and shopping malls in Beijing, Shanghai, and Guangzhou. Overcapacity and new debt problems for the banks are the result.

JOB As state-owned enterprises pile up losses, more are shutting factories, producing new jobless masses—maybe twice as high as the official statistics.

appeals to ease up on his fight against inflation until the Asian crisis was well under way and its implications for China were clear. But by December, he realized that China's own economy could stall disastrously if he didn't step on the gas, risking the ire of die-hard conservatives who oppose any increase of inflation and deficit spending. Perhaps in antic-



THREE CORGES BAN PROJECT To finance such megaprojects, the government will have to go deeply in

of his new role as Premier, Zhu has been having pathetic meetings with unemployed workers. Party members are steeling themselves for a more fundamental reform of China's state-run capitalism. The country needs a modern banking system, not the profligate mode of state-directed credit it has now. The Chinese treat foreign investors as genuine partners and not as mere sources of cash and technology. And the government realizes that the easy days of export-led growth are ending and that the task of building a domestic economy is ahead.

What's amazing is how swiftly the Asia crisis has undermined China's growth formula. Under Deng Xiaoping, Beijing and the coastal provinces invest willy-nilly in hundreds of thousands of real estate and manufacturing ventures. The doggles and corruption were astounding. Zhu finally ended cutting off the flow of cheap bank loans to pet projects. The austerity drive left even many sound companies starved for funds and forced to lay off workers. But Zhu and his leaders figured that as long as export industries remained strong, the economy would keep growing briskly. Officials figured they would have years to fix the state sector and perfect their brand of red capitalism.

But export growth may slow to 5% this year, from 22% in 1997, and cities from Beijing to Shanghai are feeling the pinch. The coastal factories, many of them started by

the go-go party cadres, are having trouble finding buyers for all their low-grade air conditioners, vacuum cleaners, and consumer electronics.

Consumer demand is dropping fast, and many retailers are desperate for shoppers. At Beijing's new Cofco Plaza shopping center, for example, the top two floors are empty of shops. And the designer clothes and bedding sold in the largest third-floor shop come from boutiques elsewhere in the building in order to fill up otherwise unoccupied space.

Such signs are alarming. If growth slips below 7%, the economy will not generate nearly enough jobs to soak up the 6 million Chinese entering the workforce each year, as well as the 12 million laid off by restructured state enterprises. Unemployment is expected to jump by an additional 10 million through 2001. The steel industry will dismiss a half-million workers—38% of its workforce—by 2000. The country's textile machine will probably lose 600,000 jobs in the next few years. City officials are frantically trying

to retrain these former factory hands, many of them over 40.

Chinese policymakers know that a significant slowdown could force them to devalue their currency. That would send a new jolt through the world economy. Devaluations, warns Zhu Min, an economic adviser to the Bank of China's president, would lead to "export wars in the second half of this year and a vicious cycle of depreciations." A slowdown could also trigger the kind of social unrest that horrifies China's leaders. And if China slides into stagnation, the world loses one more important source of growth.

FEUDING PLANNERS. That's why reigniting growth is a central part of the new plan. But don't expect to see a lucidly packaged, well-organized stimulus program emerge from the Congress. Instead, the cadres will unveil remedies piecemeal as disagreements rage over the details. Even the official *China Daily* newspaper is reporting the debate among technocrats over the wisdom of abandoning fiscal rigor and risking the creation of another bubble. Sinologists say current Premier Li Peng favors only a 10% increase in government spending, below Zhu's target. Yet, at the end of the day, analysts expect the government to boost its spending on public works and other projects as much as 20% a year.

Much of this is to come from vast personal savings—some \$560 billion piled up in state-run commercial banks throughout the country after a decade of economic growth. The goal is to ladle this money into everything from Beijing's fourth ring road to Shenzhen's subway to such megaprojects as the Three Gorges and the Yellow River's Xiaolangdi dams. The usual way to capture these savings would be to issue bonds. But ordinary Chinese investors have traditionally steered clear of long-term debt instruments, either because interest rates are low or because it is too difficult to sell them on a secondary market. Banks also are not eager to see a major bond market, which could divert funds from their deposits and make it more difficult to carry their estimated \$240 billion in dud loans.

Yet policymakers are actively debating several bold



The risk is that China wastes its savings on projects that fail to develop a market economy



may increase 20%

Cover Story



EDIFICE COMPLEX *Bank portfolios are stuffed to bursting with real estate loans*

ideas that could vastly expand China's debt markets. One would be a major expansion of corporate bonds, which authorities until now have kept at under \$2 billion a year. Liu He, an official at the State Information Center, recently proposed a big increase in the number of highway and railroad bonds. A more controversial idea is to let cities and provinces sell bonds both at home and abroad, a scheme Zhu opposes because local officials could go overboard again. The central bank is also considering an expansion of the money supply later this year through new loans to commercial banks. Plans are afoot to bankroll construction of \$350 billion in apartments over three years. The central bank also would earmark loans for infrastruc-

ture projects and small businesses.

The most urgent task Zhu faces, however, is to clean up the banking system. A key first step is Beijing's recent decision to pump \$32.5 billion in capital into its four main commercial banks by issuing new state treasury bonds. This will boost banks' capital levels to meet international standards, making it easier to carry nonperforming loans, lower lending rates, and increase profitability.

The government is also making attempts to curb the rampant growth in finance companies, which were notorious for providing loans to speculative investments. Computerization of bank data is making it easier for regulators to monitor loans. Zhu also wants to dramatically reduce the number of branches of the People's Bank of China to lessen the chances of local meddling. Top bank executives at the regional level now are appointed directly by Beijing and no longer report to provincial governments or party officials. Wang Qishan, former president of China Construction, has been named Vice-Governor of Guangdong Province, where he will try to ensure that local cadres don't dictate bank lending.

GREEN LIGHTS. Beijing will also sweeten terms for investors from the U.S. and Europe. "When the economy is bad, the authorities are polite to people like me," says William A. Hanbury Tenison, chief representative of Jardine Fleming Securities Ltd. in Shanghai. "At the moment, people are very polite."

They're about to get even nicer. Chinese authorities will soon sign off on major infrastructure projects involving Western multinationals that have been bogged down for years. In February, for example, Royal Dutch/Shell Group finally got the green light for a \$4.5 billion chemical complex, China's biggest foreign investment ever. Jack Perkowski, chairman of Asimco, a direct-investment fund with 17 joint ventures across China, is currently negotiating two more ventures, which are suddenly going more smoothly. "For everything in the contract, we're finding more flexibility now. We're seeing tangible signs," he says.

Reforms aimed at streamlining China's stifling bureaucracy would improve the investment climate immensely. Reducing the power of the Ministry of Post & Telecommunications, which both regulates and operates most of the telephone system, would help open China's phone market. Limiting the ministries' role in industry also could weaken China's ability to impose onerous rules on technology transfer and local content.

Beijing may even make it easier for foreigners to turn a profit, something it has not cared much about. Watch for new low-interest loans and reduced tax rates for particular infrastructure projects built by foreign joint ventures.

Ambitious stuff. But will it be enough? A good clue will be

China tackles its banking problem. Although Western analysts praise the \$32 billion capital injection as an important first step, "in terms of solving the problem, it's only a fraction of what they need to do," says Standard & Poor's analyst Wayne Gee.

China's banks probably need a much more massive injection of new capital so that they can write off bad debts to enterprises. Western economists also fear that China's short-term foreign debts—the Achilles' heel that brought Thailand and South Korea—may be understated. Officially listed at \$15 billion, the real figure could be several times that if the offshore borrowings of Chinese corporate entities in Hong Kong and the U.S. are included. Beijing's \$140 billion in foreign reserves is still a comfortable cushion, but China may be more vulnerable to an external financial shock than it thinks.

CAN MODEL? Throwing money at the banks won't work unless they also start lending on the basis of credit analysis, rather than politics. Also lacking so far is a comprehensive plan for the banks to wipe bad debts off their books, which is necessary if they are to stand on their own as profit-making institutions. China does not have a legal framework for banks to seize corporate assets and sell them off to outside investors. And because there is no insurance program to protect depositors, shutting down bad banks is difficult. There isn't even a system to monitor the assets of state banks. All of these issues are now being debated actively in the Chinese press, but decisions aren't expected in the coming months.

The government also has not figured out what to do with the largest state-owned enterprises, the biggest money-losers in the system. Beijing has been urging strong state companies to buy up the weaker ones to create conglomerates modeled after South Korea's *chaebol*. The well-run Baoshan Iron & Steel Corp. in Shanghai, for example, is being strong-armed into buying a poorly run metallurgy company, while Beijing's Snow Lotus Cashmere Co., one of the profitable textile makers, may have to acquire other, money-losing cashmere producers. "We are being encouraged to take over a hurting enterprise, but I'm not sure that that is a sound strategy," says General Manager Li Yuanzheng.

The crisis of Korea's *chaebol* may well force Beijing to abandon this model and even to rethink the party's emphasis on large corporations. Now, policymakers are exploring special loan funds for smaller businesses, and they may make it easier for private enterprises to issue stocks and bonds. Ready cash raised in 1997 from Hong Kong's securities markets was supposed to ease the pain of restructuring state-owned behemoths. But that money has now dried up. So the government plans to approve \$3.7 billion worth of initial offerings in China's domestic markets this year, a sum that may grow. Trouble is, regulators fear that if failing companies manage to list, the already shaky credibility of China's bourses will be undermined further.

Opening up the interior of China to serious economic development could offset the slowdown in exports and boost demand for locally made goods. Beijing is hoping its ambitious public-works program will spread the wealth to such interior cities as Wuhan and Zhengzhou. They also want to help the three-quarters of China's population that lives in rural areas but who account for only 45% of retail sales. The average annual income of a Chinese farmer is a mere \$250, whereas city residents pull in about \$620. But this will take years: The roads and power generators must be built before industry moves en masse to the hinterland.

Give credit to Zhu Rongji and China's ablest bureaucrats for recognizing a developing crisis and mobilizing to solve it. Outsiders applaud his ambition. "Zhu is shooting for the moon, but even if he ends up only half way there, it will be a tremendous acceleration of what we have seen so far," says Nicholas R. Lardy of Washington's Brookings Institution.

Yet Zhu and his colleagues have only a few years to reignite China's economy with public works and public debt. If they succeed, China's economy will be vastly more market-oriented but with the party still at the helm. If they fail, China will have the same problems it has today, except it will have a lot more debt and far fewer options. Six months ago, the Chinese thought they could avoid the fallout of the crisis. Today, the crisis is already forcing major change in Asia's most dynamic economy.

By Joyce Barnathan and Dexter Roberts in Beijing, Mark L. Clifford in Shanghai, Bruce Einhorn in Guangzhou, and Pete Engardio in New York



Many of the banks have stopped lending, choking off credit to the worthy and reckless alike

China's Financial System

THE OLD WAY...

Beijing and local officials channel bank credits to state-owned businesses.



中國人民銀行

...AND HOW IT MAY CHANGE

Beijing uses bonds to tap \$560 billion in personal savings to back big public works, boost growth, and support strategic industries. Commercial banks are freed from political influence.



DATA BUSINESS WEEK

COMMENTARY

By Gail Edmondson

'I'M SHOCKED! THERE ARE PEOPLE WORKING IN HERE!'

Imagine a country where a chief executive could be jailed because his managers work more than 39 hours a week without overtime pay or compensating time off. These aren't factory workers, but the well-paid people who in most countries rack up workweeks of 50 hours or more in offices and rarely take their full vacation. Where might that kind of regime earn the boss a prison term? *Mais, c'est la France!*

As the Socialist government of Prime Minister Lionel Jospin debates a 35-hour workweek, France has focused much attention on working hours. Officials are now enforcing the current 39-hour rule, which applies even to managers, with renewed vigor. The labor-market police unit, the Inspection du Travail, has been raiding companies to catch finance managers, engineers, software programmers, and marketing executives who, in violation of the law, work past 7:00 p.m. without keeping records of their overtime—and without compensation. *Quelle horreur!*

"FASCISM?" Thousands of citations have been issued, threatening CEOs with fines up to \$1 million and maximum jail terms of two years. Electronics giant Thomson-CSF, furniture maker Ikea, and retailer Auchan have been forced to introduce time clocks for managers. In Thomson's case, such a move settled 6,057 citations in December.

At telecom giant Alcatel Alsthom, management protested in early March. In raids on subsidiary Alcatel CIT, inspectors interrupted executives with clients and harassed engineers, who complained they were brutishly herded into an interrogation area. Alcatel's managers denounced the "administrative fascism" of the union leaders who invited the inspection and the officials who conducted it, comparing their behavior to that of

Nazi storm troopers. The union, the CFDT, which is loosely aligned with the governing Socialists, has sued for defamation.

With unemployment stubbornly high, the Jospin government's response is to redistribute work. And because that is considered the moral thing to do, Paris has considerable backing. But divvying up the pie into ever smaller pieces seems to be the sum total of the Socialists' creativity.

It's a sad tally. The intent of the 35-hour workweek

weeks for a fixed salary? While Thomson's managers take weeks of compensatory time off, rivals will eat their lunches.

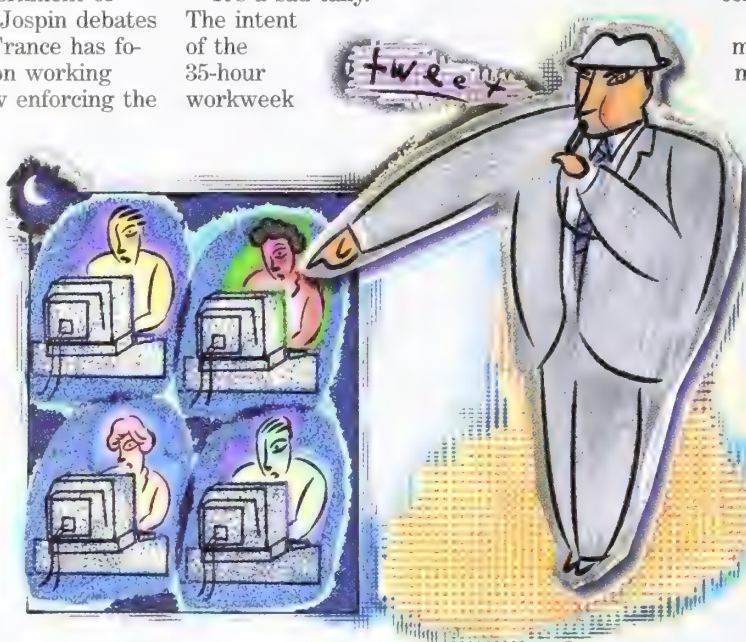
TREADMILL. Indeed, a rising number of French workers are bolting for opportunities abroad—where managers might put in 12-hour days but reap a pile of stock options. Foreign companies provide incentives for hard work, instead of relegating workers to a treadmill that honors the lowest common denominator.

If reason prevails, lawmakers will separate managers from hourly workers as they debate the 35-hour workweek. Labor Ministry officials, taken aback by the aggressive raids of workplace inspectors, acknowledge the need for separate rules for managers. Industry leaders hope to break the straight-line equation between hours and compensation. Instead of paying overtime for hours in excess of the limit, companies would offer a package of benefits, such as training programs and additional vacation

days, for a manager's more demanding duties. In 1984, IBM France negotiated an agreement like this. Under it, managers can receive two or three days per quarter in extra vacation, at the discretion of their superiors, for excessive overtime.

French managers are no strangers to overtime. One survey indicates that half of them work more than 46 hours a week—and 25% more than 51. Accordingly, some unions say managers should get an additional five to six weeks of vacation a year, bringing the total to 10 to 12 weeks—almost one week in four. Imagine how many companies would remain in France then.

Edmondson is Paris bureau chief.



and the raids is to force new hiring. If you have to pay a software engineer 100% more because he works 60 hours a week, why not hire another engineer? But dividing up existing wealth won't create new wealth. Controls on the labor market won't encourage companies to invest or startups to launch businesses. "The government has to think more about the needs of a service economy," says Bernard Dufau, president of IBM France. "They're imposing more rigidity when what's needed is flexibility."

The false assumption is that France's economy can operate in a vacuum. How should Thomson-CSF compete with Lockheed Martin Corp. when U.S. managers can log 60-hour



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COMMENTARY

By Robert Neff

ARE JAPAN'S PROSECUTORS ON A SECRET MISSION?

The Japanese had only gotten over the shocking suicide of parliamentarian Shokei Arai when they got more disturbing news. Authorities were investigating Eisuke Sakakibara, Japan's vice-finance minister for international affairs, for allegedly pressuring Daiwa Securities to cover an associate's losses.

Sakakibara denies the charges, and things may blow over. But with such a high-placed name being dragged into the swirl of financial scandal, the Japanese realize that these investigations are getting serious. That's not to say the Japanese expect an end to the suspect behavior that connects the politicians and ministries with the businesses they are supposed to regulate. Says a Japanese fund manager: "It's just *tokage no shippo kiri*"—cutting off a lizard's tail. Lop off a few corrupt officials, and the system will generate others. Yet these investigations do show how the Japanese power system is at war with itself—and creating an ambiguous environment that few but the savviest insiders can navigate.

EASY PICKINGS. Take the case of Arai, a dashing, self-styled reformer. He apparently did what many Japanese politicians do. He allegedly pressured Nikko Securities Co. to guarantee him stock profits. Although prosecutors seem to have the goods on many politicians, they chose to go after Arai. Why? Because he was easy pickings. The first and only Diet member of Korean descent, he had few strong protectors, and he had abandoned the ruling Liberal Democratic Party for a while to join a new "reformist" party. When he came back inside the LDP fold a few years ago, none of its powerful factions would accept him.

Worse yet, as a former elite bureaucrat at the Ministry of Finance, Arai suited the prosecutors' recent campaign to rein in MOF. Even as they were chasing Arai, the prosecutors were zeroing in on MOF officials for allegedly indulging in *settai*—winning and dining with executives who



TARGET: Arai shortly before his suicide

picked up the tab in exchange for sensitive information.

Some observers believe that the prosecutors genuinely worry that MOF is jeopardizing their country. Given the MOF's bungling of economic policy and financial regulation, "the prosecutors' intention is to save and protect Japan's bureaucratic system," says Takao Tshikawa, special correspondent for the monthly *Oriental Economist*. But because they are facing off against the combined might of the LDP and MOF, the prosecutors have so far only been able to pick off stragglers like Arai.

This guerrilla war is likely to drag on, since MOF cannot stop these investigations completely. Moreover, conflict inside MOF may give the prosecutors more openings. MOF officials

themselves are conducting the investigation of Sakakibara, who has his rivals inside the ministry. If the investigation expands, the prosecutors may eventually get a piece of the action.

The prosecutors are formidable adversaries and are accountable only to themselves. The prosecutor-general outranks the Justice Ministry's top administrative minister and answers only to a commission of other top prosecutors. Because of reverberations from a previous attempt by a Justice Minister to intervene in prosecutorial activities, "it is very dangerous for politicians to tell prosecutors what to do," says political commentator Minoru Morita.

STALEMATE. What is more, one-time law-enforcement officials are gaining power. Former prosecutors and judges now run five key financial-industry regulatory agencies.

Another new watchdog agency appears likely to be headed by a former prosecutor. And new Finance Minister Hikaru Matsunaga served as a prosecutor before turning politician.

The result of all this will probably be a stalemate. The prosecutors will keep pushing, while MOF and the LDP will not fundamentally change. But the prosecutors will succeed in creating new ambiguities in the Japanese system. By defining *settai* as bribery, they are calling into question a practice that has flourished for centuries.

For foreign companies in Japan, this development just adds to the difficulty of understanding what's acceptable in business. "It isn't clear what the rules are," says Glen Fukushima, president of the American Chamber of Commerce in Japan. "Even if transparency is formally increased, personal relationships in Japan being what they are, newcomers often are forced to take unconventional measures to compensate." Meanwhile, he suggests, Japanese players will prove savvy at adjusting to the new rules, unclear as they are. And that, perhaps, is how the Japanese like it.

Contributing Editor Neff covers Japanese politics and finance.

Rooting out corruption
may be secondary to
curbing the power of
the Ministry of Finance

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EDITED BY JOHN TEMPLEMAN

OLD-STYLE POLITICS COULD SINK THE NEW KOREA

Little more than a week into his five-year term, South Korean President Kim Dae Jung is under siege. The opposition Grand National Party refuses to confirm his Prime Minister, Kim Jong Pil. Worse, the GNP is intent on challenging Kim's crusade to institute radical reforms to pull South Korea out of its economic crisis.

Gridlock is threatening to snarl up Korean politics, weaken Kim's presidency, and crimp his ability to manage the crisis. Kim, of course, holds some trump cards. He has strong international backing and an electoral mandate for change. But the GNP controls 161 of 294 seats in the National Assembly, which must enact key reforms to accountancy, bankruptcy, and corporate-governance standards. Analysts say the faction-riddled GNP is more worried about losing its majority by attrition than it is about backing reform.

ERSTWHILE ENEMIES. Kim is fighting back by working up political countermeasures that would weaken his opponents. And he is thumbing his nose at the GNP by naming Kim as his acting Prime Minister, a move that doesn't need parliamentary approval. But the brawling could put essential reforms on hold.

Partisan politics is a luxury South Korea can ill afford. Unemployment soared to an 11-year high of 4.5% in January and will head higher. The won's blowout has pumped inflation to near double-digit levels. And the economy will be lucky to grow 1% this year. Now, in exchange for a \$60 billion bailout, Kim must implement an International Monetary Fund austerity program. He had hoped the GNP would help—at least initially—to build a consensus to reform the vast industrial *chaebol*, shutter insolvent banks, and brace the public for hardship.

But the GNP, formerly the ruling New Korea Party of outgoing President Kim Young Sam, is fighting every inch of the way. The party is friendlier to the *chaebol* and Seoul's

debt-besotted banks than is the President. It may stymie measures that threaten business barons or its own campaign coffers. "The reform process is faltering while our core problems have not been tackled," frets Park Kyung Suh, research fellow at the Korea Institute of Finance think tank.

So far, Kim, 74, shows no sign of ditching his acting premier. The irony is rich. Kim Jong Pil backed the coup that brought strongman Park Chung Hee to power in 1961. He founded the notorious Korean Central Intelligence Agency that allegedly tried to kill Kim Dae Jung, then a dissident.

But as rival candidates last December, the erstwhile enemies made common cause.

FEAR OF DEFECTIONS. The GNP argues that it opposes Kim Jong Pil out of principle. "[He] symbolizes an old era when corruption was rife," intones GNP lawmaker Lee Shin Bom. Truth is, the GNP is terrified that its own members will defect to the Kims, who want to adopt a parliamentary system giving lawmakers more power. Legislators love the idea, which could bring pork to their constituencies. "A debate on constitutional changes could split [the GNP]," warns Gong Sung Jin, head of the Hanbek Foundation think tank.

Meanwhile, economic reform is bogging down. President Kim had cajoled the *chaebol*

into accepting changes. They agreed, for instance, to end cross-lending among subsidiaries, adopt transparent accounts, and divest nonessential businesses. Yet when Kim's party introduced a bill during the presidential transition to permit foreign hostile takeovers immediately so as to speed the process, the GNP pushed back the start date to 1999.

It seems that not even the biggest economic upheaval since the Korean War can focus the nation's leaders on unity. South Korea, as a result, could end up paying a far higher price in economic pain than it needs to.

By Moon Ihlwan and Brian Bremner in Seoul



KIMS: President and Premier

GLOBAL WRAPUP

GERMAN PAY TALKS GET TENSE

► With German unemployment nearing 12%, the bargaining over municipal workers' pay was bound to be tense. But the Mar. 2 nomination of Gerhard Schröder as the Social Democratic Party's candidate for Chancellor in September is adding spice. Striking garbage collectors and bus drivers are demanding 4.5% wage hikes, perhaps emboldened by the prospect of a new government.

But economists say the workers are likely to get only inflation-matching

raises of 1.5% to 2%. State and local governments will hang tough because their deal will set the benchmark for other contracts this year, including those in retail and construction. Union leaders may go for a modest, short-term contract now, hoping to win a better deal if Schröder wins.

A MALAYSIAN BANK BAILOUT?

► Malaysian ruling party United National Malays Organization is mulling a bailout of the politically wired Sime Bank, Kuala Lumpur analysts say. Local stock markets went

into a funk on Mar. 4, after the bank reported \$431 million losses for the six months through Dec. 31. They took the news as a sign that Malaysia's financial system is in far worse shape than earlier thought.

Sime Bank is controlled by two investment funds linked to UNMO. It has ties to Prime Minister Mahathir Mohamad's closest economic adviser, Daim Zainuddin, who once had a big stake in parent Sime Darby. Odds are another Mahathir confidant, Rashid Hussein, would lead a bailout by merging Sime Bank with his Rashid Hussein Bank.

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WHY AVON CALLED 'NONWOMAN'

Replacing Charles Perrin as CEO, the board decided its female execs just weren't ready

Ann S. Moore, *People* magazine's high-profile president, is familiar with juicy stories. But she never dreamed her board seat at Avon Products would land her in the middle of one. In February, as she walked into a Sunday luncheon for Anna Hanover, wife of New York City Mayor Rudolph W. Giuliani, she drew more attention than such guests as Tom Lucci and Joan Rivers. "So how 'bout that biggle Avon CEO?" Hanover chided. Moore, in December helped ease Avon's new leader, Charles Perrin, into the job. "No," she says today.

This isn't the reception he expected when it was announced that Perrin was the new chief executive. He had led DuraCell International Inc.

through solid global growth since 1993 and was up for several CEO jobs last year. After Gillette Co. bought the battery-maker, Perrin, 52, became the pivot piece of a broader succession plan: Andrea Jung, a 39-year-old marketing executive, became president and Perrin's designated successor. She got a board seat, as did Susan J. Kropf, Avon's first African American president and a direct-selling veteran. "I went to bed thinking I had made this cosmic move," Moore says. "I woke up speechless."

In the morning, Avon was blasted for missing an opportunity to give a woman a shot at running the corporation—one that derives its \$5.1 billion in sales from an army of women selling everything from lipstick to lacy lingerie.



"Where would Avon be without women?" demanded Susan Bianchi-Sand, an equal-pay advocate, on TV. Across the Atlantic, the *Daily Telegraph* declared: "DuraCell man powers past Avon ladies."

Insiders and analysts derided Perrin's lack of direct-selling background. The clincher came last month, with the resignation of Christina A. Gold, 50, an Avon executive vice-president many outsiders believed was a leading candidate for CEO. "There's a reason they chose me," Perrin laments. "All anybody knows is that I am the nonwoman."

MAKEOVER TEAM

Perrin (right) will work with Jung, Kropf, and Preston in guiding Avon's shift into a global brand

How did one of the most women-friendly companies in America become a poster child for the glass ceiling? A reconstruction of Avon's search shows that despite a decade of putting women into high executive posts, when the CEO

job came open, the board concluded that none yet had the experience or skills to lead Avon in a new direction.

Once the embodiment of door-to-door sales, Avon wants to remake itself into a glamorous brand sold worldwide to upwardly mobile baby boomers and hip twentysomethings. To guide the shift, Avon sought a CEO who had already

The Corporation

run a major corporation or unit—and who had proven experience establishing a global brand. Just as important, the new CEO had to be able to fit into a touchy-feely culture that has rejected several outside execs. “We found only about a dozen people who fit the bill,” Moore says.

To many outsiders, it sounds like the same old story: A woman is good enough to be a specialist or a strong No. 2 to a male CEO, but never good enough to be No. 1 herself. To the five members of the search committee—including two accomplished female executives—Avon is being pilloried for putting corporate needs ahead of gender politics. “As a woman, I can defend this decision to anybody,” says Brenda Barnes, an Avon director, who took herself off the list of prospects when she quit her post as president and chief executive of Pepsi-Cola Co. North America to devote more time to her family. “It would have been great to have found a woman. But we did what was best for Avon.”

JILTED. The search started in May, when Edward J. Robinson, Avon’s president, resigned over a succession disagreement after the board asked CEO James E. Preston to postpone retirement. With six freshly minted female executive vice-presidents, Wall Street and women’s groups speculated that Avon’s next chief would be female. They singled out three names: Gold, Jung, and Kropf. “Everyone fell in love with the idea of a woman running Avon,” says Gail Blanke, who built and then bought out a work/family consulting unit at Avon. “When people fall in love with an idea and it doesn’t happen, they feel jilted.”

Avon officials say they tried to squelch the hype, without success. While they considered several inside candidates, only Jung and Kropf were interviewed, they say, as were two men. “I told reporters that if they painted this as a three-way horse race they’d be wrong,” Preston says. “They chose to ig-



nore me. I said that in my lifetime a woman would run Avon. I never said the next CEO would be a woman.”

Not in so many words. But it was Preston’s widely publicized female fast-tracking that created the impression that at Avon, women were poised to rocket through the glass ceiling. When he became CEO in 1988, Avon’s top ranks were dominated by men. Blaming Avon’s financial woes on a lack of female input, Preston elevated a slew of women and drove home the message by giving up corporate baseball seats and hunting-club memberships and buying season tickets to the ballet and New York Philharmonic.

After Avon’s latest restructuring, women hold a third of its officers’ jobs and half of the board seats. According to Catalyst, a research and advocacy group for businesswomen, the average U.S. corporation has just one female director, and only 10.6% of officers are women. “They are an exceedingly good company for women—one of the best,” Catalyst President Sheila W. Wellington says.

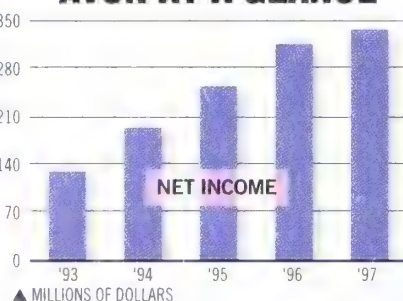
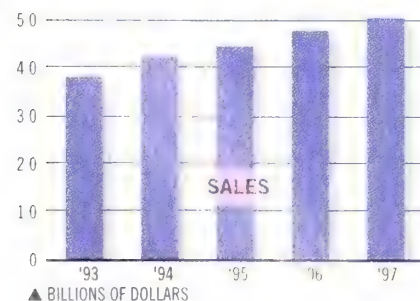
SNUBBED Gold opted for a staff post—and sent the wrong signal

operating division, guaranteed that only a handful of women in America could even be candidates. There are only a few female CEOs of major U.S. companies, such as Jill Barad of Mattel Inc. and Marion Sandler, who shares the top post at Golden West Financial Corp. with her husband, Herbert. And women hold only 5.3% of line management positions—overseeing manufacturing or handling profit-and-loss duties—which are key to most senior promotions, Catalyst says.

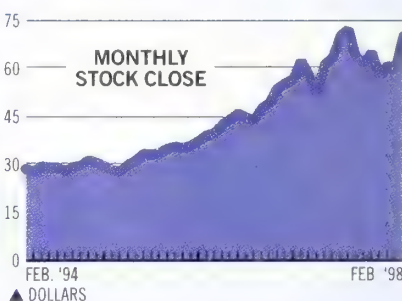
“SIX DEGREES.” “We were all aware of the woman image issue thing, and all things being equal, or almost equal, we would have wanted a woman,” says Edward T. Fogarty, the former Tambrands Inc. chief executive who led the hunt with Moore, Barnes, Readers Digest Association Inc. Chief George V. Grune, and Charles S. Locke, the retired head of Morton International Inc.

The team did not hire an executive search firm. Instead, the board relied on its own connections. It evaluated a list of well-known female executives, from Lois Juliber, the head of operations at Colgate-Palmolive, to Ann M. Fudge, president of Kraft Foods’ coffee and cereals division, and Ellen R. Marram, CEO of Seagram’s Tropicana Beverage Group. Several of the directors had worked with each of these well-known female candidates personally. “This is six degrees of separation,” says Moore. “There’s not a woman you can name whom we don’t know well. The reason Brenda Barnes and I were put on the board was to make sure the

AVON AT A GLANCE



DATA: AVON PRODUCTS INC., BLOOMBERG FINANCIAL MARKETS



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"It would have been great to have found a woman. But we did what was best for Avon," says director Brenda Barnes

Ann Fudges of the world got due process. Although she would not assess each female prospect, Moore says: "We are all in our 40s, not in our 50s, with international experience. And one of the criteria was, 'Do you want this job?' This is a hard job. We not only needed someone with experience, we wanted someone ready, willing, and able."

Several search firms acknowledged that their list of Avon candidates would not have been much broader. "We'd have the same list of 10 or 20 people, because of their specific needs," says Dale Winston, president of Battalia Winston International, a New York search firm. In the end, Moore says only one person came out on top in each of the criteria: Charles Perrin. He was, in fact, considered for the top jobs at Quaker Oats Co. and Campbell Soup Co., says Thomas J. Neff, the SpencerStuart executive handling those searches.

HOT TICKET. Why was Perrin such a hot ticket? From 1993 to 1997, when he was CEO of Duracell, its market capitalization rose from \$1.8 billion to \$9.4 billion. He transformed Duracell from an American brand to one that cornered half the world battery market. For Avon, he had another important quality: After working with him on Avon's board since May, 1996, Preston believed Perrin's personality would mesh well with the corporate culture. "We didn't want an Al Dunlap," Preston says. Still, having come from what Perrin describes as a "manly man" culture at Duracell, he has had to work hard to adjust.

Perrin's personality, in fact, was researched as deeply as his track record. The search team talked to dozens of employees and executives and grilled Perrin over meetings, dinners, and lunches. They probed his record at Chesebrough-Pond's USA Co., where in 12 years he rose to president of packaged goods. "Brenda and I called women who worked for him to see how sensitive he was to them," Moore says.

At the same time, they interviewed Jung, Kropf, and Jose Ferreira Jr., the president of the Asia-Pacific region, who joined the company in 1980. Jung, with a heavy mar-



keting background, lacked experience running all aspects of a business. In 27 years at Avon, Kropf ran units in Central Europe and Russia but was short on marketing experience. Ferreira needed brand-building skills. All three say they agreed with the decision. "Never for a moment did I expect a call saying, 'Susan, you're the next CEO,'" Kropf says.

One name was conspicuously absent from the internal candidates: Christina Gold, who was dubbed the "Golden Girl" as she rode Preston's promotion wave. Fresh out of college in Toronto, Gold started as a clerk in 1970 and climbed through the ranks to run Canada. Preston was so impressed that when the U.S. unit, with a third of Avon's revenues, hit a wall in 1993, he tapped Gold as its first female president.

The sales force was in revolt because their incentives had been chopped and they were being bypassed with a new direct-mail catalog. About 25,000 Avon ladies left, pulling profits down 30%. Gold sweetened rewards and added apparel and gifts, pushing up noncosmetics sales in two years from \$140 million to \$765 million and rebuilding the ranks.

Last year, the job was turned over to Kropf during a major shuffle designed to round out top employees. Gold was offered a job managing operations in several countries but turned it down for a job on the corporate staff analyzing what direct-selling practices worked best worldwide. She saw it as a move up. "I ran the biggest part of the corporation—the one with the most profits," Gold says. "I felt I had proven myself." But Moore says the board saw her choice as a signal that Gold was stepping out of the succession race.

"Brenda and I looked at each other and said, 'What is she thinking?'" Moore recalls. "She took herself out of the running for CEO."

Gold says that was not her intention. The job she took, after all, was critical, given that 98% of Avon's business still comes from direct selling. But it was not central to Avon's new strategy. The company is spending hundreds of millions of dollars on new ads, marketing, and product development to develop the sort of international name recognition enjoyed by Coke or McDonald's—as Perrin did at Duracell. Avon wants to sell on the Internet, through 800 numbers, and in chic stores like the spa and "image center" it is opening at Trump Tower in Manhattan.

"Christina had a lot of direct-selling experience," Preston says. "But we're steeped in direct-selling experience. We're going through enormous change. We needed a change in leaders." Gold resigned abruptly in February.

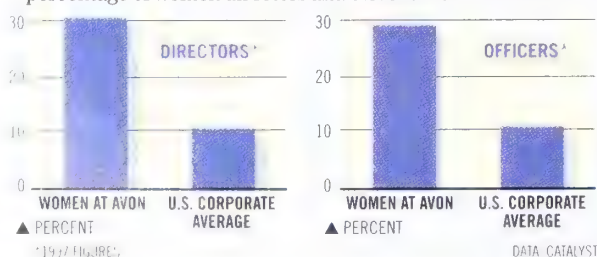
Avon's shift in direction was masterminded by a young woman who worked for Gold and then leapfrogged her. Andrea Jung, born in Toronto to Chinese immigrants, rose from Bloomingdale's management trainee to Neiman Marcus Co. exec before heading marketing at Avon in January, 1994. "The new strategy was very much Andrea's creation," says Preston. Chic and high-powered, the Princeton graduate wiped out 30% of Avon's old products and added six global brands. By 2000, the moves are designed to position 70% of Avon's products to sell consistently around the world. "She has a unique combination of left-brain, right-brain—creativity and business," says Donna Karan, who put Jung on her own board.

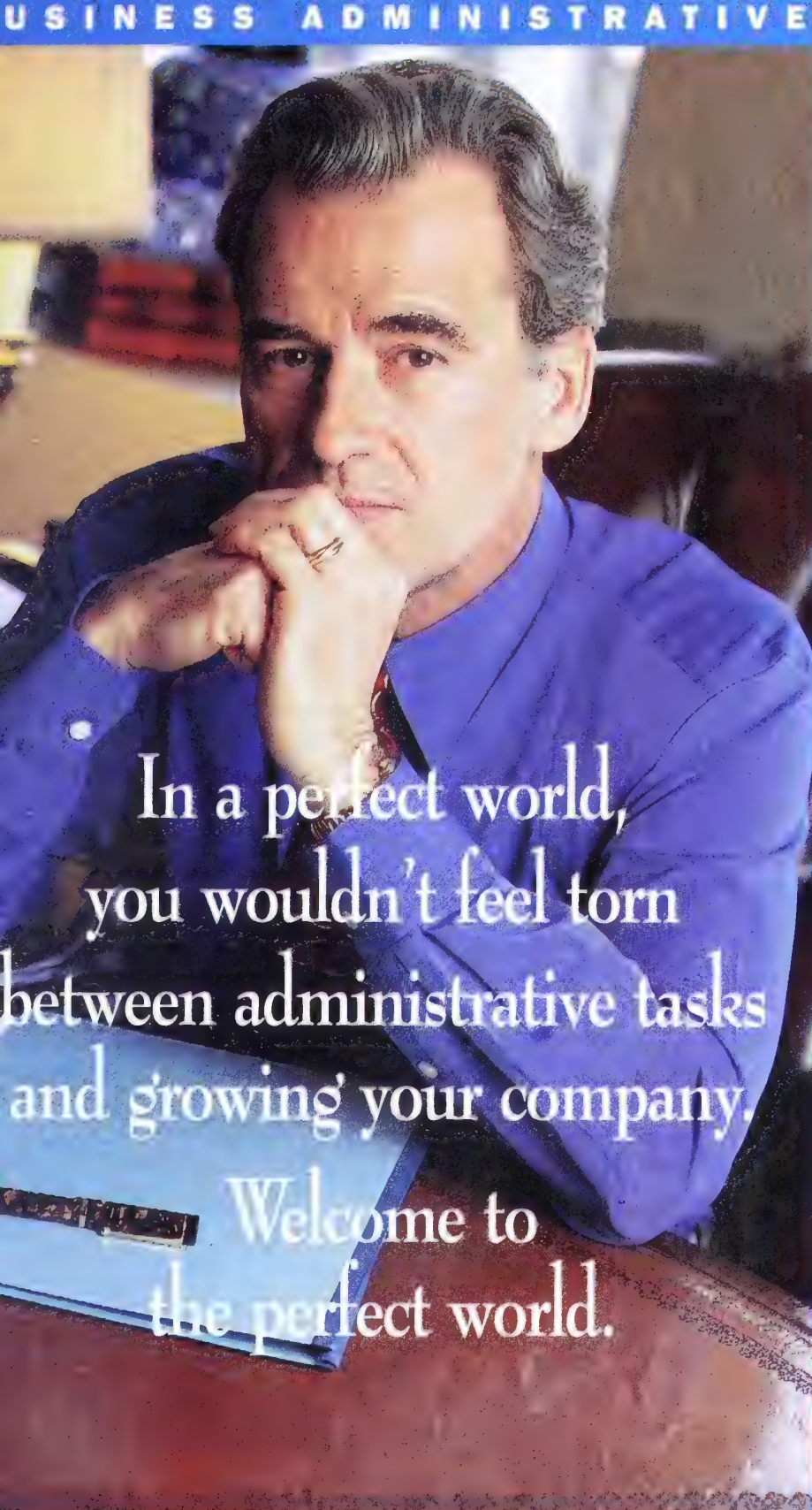
Today, Preston says, Jung is the "clear heir apparent." With Jung and Kropf on the Avon board, fellow directors should have a chance to gauge their thinking and personalities—as they did with Perrin. But anything can happen between now and 2005 or so, when Perrin retires. As Avon's CEO saga proves, even when the path to the top is paved with good intentions, there's no telling who will win the race.

By I. Jeanne Dugan in New York

AVON: A WOMAN'S PLACE

Among the 500 largest U.S. companies, Avon ranks fifth in percentage of women directors and eleventh for women officers





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COMMENTARY

By Kathleen Kerwin

WHY DIDN'T GM DO MORE FOR SATURN?

Tom Sawyer would be amused by Saturn. The carmaker's recent TV commercials show cheerful workers and managers, side by side, painting fences outside their Spring Hill (Tenn.) factory. What the folksy ads fail to mention is that workers took up their brushes only because Saturn's cutback in production of slow-selling small cars last fall left them with plenty of time on their hands.

Saturn workers may have time for a lot more sprucing up this year. Sales at General Motors Corp.'s show-case car division were down 20% in January from a year earlier, after tumbling 10% for all of 1997. First-half output has been slashed by 21,000 cars, or 14%. And workers, dissatisfied as their bonuses shrink with sales and profits, will vote on Mar. 10 and 11 whether to revoke their ground-breaking cooperative labor pact.

VICTIM? GM execs just shake their heads and argue that Saturn is a victim of the dwindling small-car market. "The market for small cars has just dried up completely," says GM Chairman John F. Smith Jr. That's certainly true—as far as it goes. To get around the slump, GM is counting on sharper marketing. It also plans to add about a third more dealerships, bringing the total to about 500.

But Saturn shouldn't be wholly dependent on small cars—and if the division comes to a dead end, GM will have squandered an epic opportunity. Give the No. 1 auto maker credit for accomplishing the hard part—launching from scratch a division that has been Detroit's one smashing, cross-generational victory in the war to win back import buyers. But rather than doing everything possible to build on that success, GM is now letting Saturn wither on the vine. It has allowed sibling rivalry to smother Saturn, delaying and denying additions to its lineup while favoring fading brands with new products.

By limiting Saturn to a single



IN A JAM: A 1994 Saturn festival attracted 44,000 owners

small car, in sedan, coupe, and station wagon versions, GM is crippling its best hope for winning and keeping new customers. Saturn needs a minivan and a larger car. With its unconventional image and the huge reservoir of good will it inspires among consumers, Saturn would be an ideal candidate to launch an innovative, car-based sport-utility vehicle, like Toyota's RAV4 and Honda's CR-V.

No other mass-market car division is expected to survive on sales of just one model. Saturn's limited lineup forces even satisfied customers to defect. Dan Nogal's family of four outgrew their beloved Saturn wagon, so a few weeks ago they traded it for a used Plymouth Grand Voyager. "If Saturn had a van or even a mid-size car, I probably would have bought from them," says the Las Vegas human resources manager. Furman Selz Inc. analyst Maryann N. Keller worries that as profits dwindle for Saturn dealers, they'll have a hard time maintaining the service standards that earned Saturn a sterling reputation.

It's that reputation that makes Saturn's woes more than just another Big Three stumble. By offering luxury-brand levels

of quality and service and forging a bond with consumers, Saturn inspired cultlike devotion. In 1994, 44,000 Saturn owners turned out in the rain for a homecoming weekend in Spring Hill.

So why is Saturn still a one-trick pony? In the early '90s, when GM was struggling to remake itself, it decided to pump billions into new models intended to revive Oldsmobile and Buick, instead of more Saturn models. There wasn't enough cash to do both, execs say. So

while GM has introduced 15 new cars and minivans in the past 18 months, Saturn's cupboard is almost bare.

Buick, Olds, and Cadillac—fettered by stodgy images they've had trouble shaking—struggle to sell snazzy new vehicles such as the Regal, Intrigue, Silhouette minivan, Bravada SUV, and Catera. Many analysts believe similar models would fly out the doors at Saturn.

In 1996, GM finally agreed to give Saturn a new, larger car—a compact sedan dubbed the LS. But it won't arrive until mid-1999. Meanwhile, Saturn risks losing more luster. Unfortunately, GM can't simply borrow a model from another division. To speed new models to market, however, it could begin designing Saturns that share a platform and key components with other GM vehicles.

GM is hinting it may eventually give the division a new SUV. Saturn needs that—plus a minivan and another larger car. Sadly, by the time those models arrive, three or four years from now, GM's upstart division already may have painted itself into a corner.

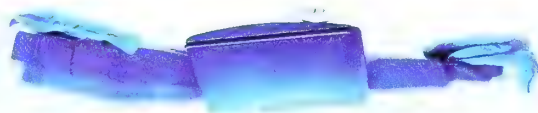
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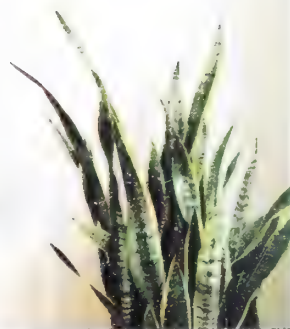
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FORCED INTO ARBITRATION? NOT ANY MORE

More employees are saying it's unfair—and many judges agree

When Marybeth Cremin joined Merrill Lynch & Co.'s broker training program in 1982, she paid little attention to the contract she signed requiring her to take any dispute with the financial services giant to an arbitrator. This "mandatory arbitration" policy, similar to those at hundreds of other companies, barred her from ever suing Merrill Lynch in court.

When Merrill fired Cremin in 1995, the then 38-year-old mother of four suddenly regretted having consented to those terms. She believes she was illegally terminated for exercising a basic right: having children. Throughout her stay at Merrill Lynch, Cremin claims, her boss demeaned her for trying to combine family and career. Finally, Cremin's complaint says, he badgered her into quitting and accepting a part-time position—which never materialized.

But even though Cremin believes she has a strong case, Merrill's mandatory arbitration policy means that she will never get a chance to seek compensation before a jury. So now, Cremin is the lead plaintiff in a sexual discrimination class action that is trying to strike down the company's arbitration program. "I didn't know I'd signed away my consti-

tutional rights," she says. "I was 21, just out of business school. I was dumbfounded when I found out." Merrill Lynch denies the allegations of sexual discrimination and contends that its mandatory arbitration policy is legal.

Cremin is not the only one crying foul. Ever since 1991, when the U.S. Supreme Court approved the use of mandatory arbitration for workplace disputes, the number of companies implementing the practice has soared. Employers praise the procedure as an antidote to runaway litigation costs. After all, 70% of the cases in mandatory arbitration are decided

CREMIN: "I didn't know I'd signed away my constitutional rights"

in favor of the company, and damages are generally lower than those in court.

Employees, though, are increasingly convinced that the system is allowing companies to break laws prohibiting sexual, religious, and racial discrimination among other things. But until recently, people such as Cremin had little chance of escaping the in-house system.

UNDER ATTACK. That's rapidly changing. For at least a year, a broad backlash against mandatory arbitration has been gaining force. Companies with policies that strip away too many employee rights are seeing their policies attacked, and sometimes disregarded, by judges, federal agencies, and organizations and private companies that provide arbitrators (table). And on Mar. 2, the U.S. Supreme Court decided to hear a case brought by a South Carolina longshoreman who is trying to break free of his employer's mandatory arbitration program to bring a disability claim. A high court ruling against the company could sharply limit the use of such policies.

While this backlash is no threat to other forms of "alternative dispute resolution"—for example, mediation and voluntary arbitration—it's forcing many employers to reevaluate the legality of their current mandatory arbitration schemes. Others that had plans to implement binding arbitration programs are putting them on hold, says New York City attorney Wayne Outten, president of the National Employee Rights Institute. "A lot of companies that have been considering mandatory arbitration are afraid of the brouhaha," he says.

The most recent blow against mandatory arbitration occurred in February, when a Boston federal judge refused to apply Merrill Lynch's policy in a sexual discrimination suit brought by a broker prior to the Cremin class action. There, the plaintiff's attorney showed that ar-

THE ASSAULT ON BINDING ARBITRATION

Although the use of mandatory arbitration is on the rise, the practice is under attack on several fronts

COURTS Judges have recently overturned policies by Merrill Lynch, Circuit City Stores, and Supercuts, among others

EEOC Officials at the Equal Employment Opportunity Commission have waged a broad campaign against mandatory arbitration, pressuring other federal agencies to discourage the practice and filing amicus briefs in civil cases

PRIVATE SECTOR Many alternative dispute resolution companies won't provide arbitrators for companies whose policies don't meet fairness standards

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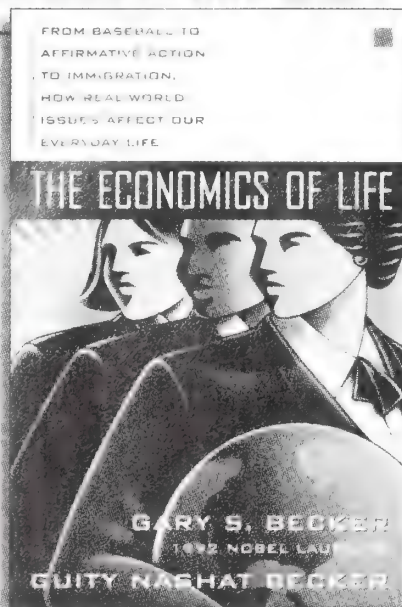
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Legal Affairs

bitrators sided with brokerage firms in 93 out of 97 cases brought against New York Stock Exchange members over the past five years. In November, meanwhile, Smith Barney agreed to give workers new rights under its mandatory arbitration policy to settle a New York sex discrimination suit.

In November, the National Association of Securities Dealers announced that it wants to delete the mandatory arbitration requirement from the form brokers fill out to be registered. Triggered by the mounting complaints about such programs, the proposal is under consideration by the Securities & Exchange Commission.

HIGHER STANDARDS. It isn't just the securities industry that's feeling the heat. In May, 1997, a Maryland federal court ruled that Circuit City Stores Inc. could not force its arbitration program on a job applicant accusing the company of race discrimination. And in January of that year, a state court in San Francisco disregarded a program of hair salon chain Supercuts Inc. because it limited employees' potential damages (the case later was settled). "Finally, some courts are beginning to say we are going to have some standards here. We are not going to just go with anything the employer tries to do," says Ellen J. Vargyas, legal counsel for the Equal Employment Opportunity Commission. Over the past three years, the EEOC has filed briefs opposing mandatory arbitration in more than 25 employee lawsuits.

Rising opposition to binding arbitration has caught the attention of the major associations that supply arbitrators for the approximately \$200 million industry. Fearful that companies will stop using the process if too many judges disregard it, they are raising their standards. Last summer, the American Arbitration Assn. issued a statement saying employment disputes are best resolved when the parties "knowingly and voluntarily agree on the process"—an unprecedented swipe at mandatory arbitration.

The National Academy of Arbitrators, meanwhile, in May issued new guidelines calling for both sides to have equal rights of representation and factual investigation. "Many employers have adopted plans [that] are quite unfair," acknowledges past President George Nicolau. That's the kind of thinking Marybeth Cremin is banking on to keep her out of arbitration. And the rising chorus behind her gives Cremin a fighting chance to get her day in court.

By De'Ann Weimer in Chicago and Stephanie Anderson Forest in Dallas, with bureau reports

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BASKETBALL

IS KOBE BRYANT THE AIR APPARENT?

The NBA needs a new king. So far, it has a promising prince



New York," reads a famous T-shirt. "It ain't Kansas." It ain't Los Angeles, either. When the image of a cherubic fan in a Los Angeles Lakers jersey flashes on the electronic gameboard of Madison Square Garden on the first day of March, the crowd erupts in a Bronx chorus of boos. So what if he's only two years old. The hooting is even louder when Shaquille O'Neal sinks a couple of foul shots against the New York Knicks. But then, a gangly teenage Lak-

er named Kobe Bryant does the same. There is silence. And later, after he drops in a three-pointer, there is applause—even scattered cheering.

It hasn't been the smoothest National Basketball Assn. season in memory: Michael Jordan, the best goodwill ambassador that basketball has ever had, is talking about putting his Air Jordans in mothballs; the Latrell Sprewell incident pointed up the nasty issue of racial tension in a league with perhaps too many abusive white coaches and too

many spoiled black athletes; and low scoring has critics complaining about tired veterans and ball-hogging hotshots who aren't playing a team game. Even NBA Executive Vice-President and Chief Marketing Officer Rick Welts concedes that this season's incidents "could damage the NBA brand," that the bond between fans and players has been "stretched thin."

All of which leads to the question on everyone's mind: Who will succeed Jordan? Who will be the new face of the NBA? Who will lead this enormously successful enterprise micromanaged by Commissioner David J. Stern into the next century? The NBA by design has been built on personalities such as Larry Bird, Magic Johnson, and Jordan, arguably the most popular athlete in the world. So the league has been groping for an Air apparent. As Welts says: "The game will continue to be driven by individual personalities and stars." But such pretenders to the throne as Shaq and Grant Hill and Penny Hardaway just don't seem to have the magic. Then there's Kobe.

If you look hard enough, you can see the future of the NBA at a tiny practice facility called Basketball City on a Hudson River pier. There, sleek, young L. A. Lakers have just finished a two-hour practice, a day before a game they would lose to the grizzled Knicks. As the players walk off the court, a 19-year-old with soft almond eyes, long lashes, and a wispy mustache and goatee is surrounded by two dozen autograph-seeking kids. Kobe Bryant, the man-child who has captivated basketball, smiles for the cameras and signs balls, jerseys, and photos of himself. Some kids get a hug.

PACKAGE DEAL. Six months shy of his 20th birthday, Bryant is having the time of his life. Even after his weak playing contributes to a 101-89 loss to the Knicks, Bryant charms the New York media wolves hungry for any sound bite. "The more you learn, the more fun you have," he tells the horde in a sweltering locker room. "Even though I hate this moment, it may be one of the best moments of my life."

At 6 feet 7 inches, Kobe is, as they say on the courts, the complete package. Capable of sailing over taller players or dribbling around the more nimble, he can score 33 points on any given night, as he did earlier this year in a narrow loss to Jordan's Chicago Bulls. In February,

ONE-ON-ONE

Bryant—facing off against Jordan in February's All-Star game—has talent and charisma, but he's just 19



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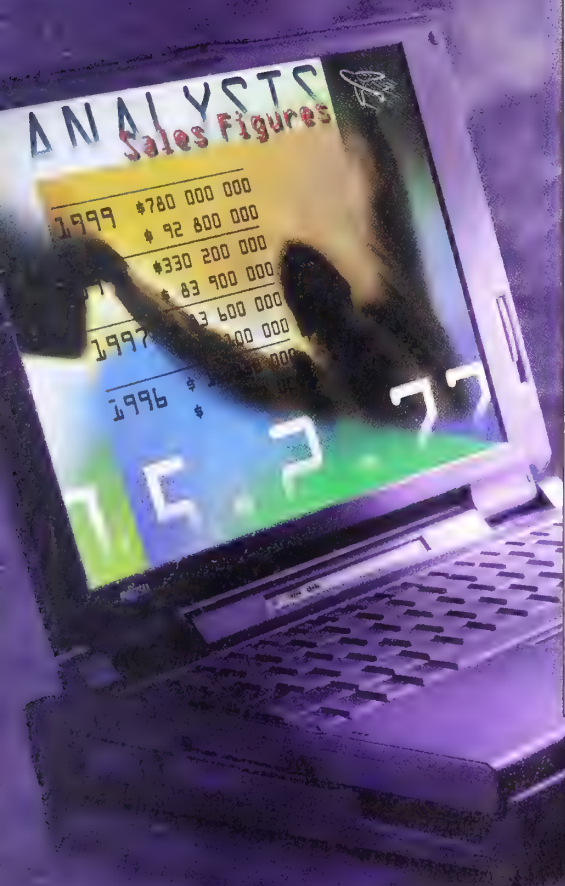
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he became the youngest player to ever start an NBA All-Star game, testimony as much to his ability as to his popularity with the fans who voted for him.

Better yet, he may be the antidote to what ails the NBA. With an easy charm and quiet charisma, this superstar-in-the-making is unfailingly polite and still lives with his mom, dad, and two sisters. In a league in which green-haired attention hogs have been known to headbutt refs, Bryant is a gentleman who says he "never thought" of getting tattoos and doesn't drink or take drugs because "my parents told me it wouldn't be good for my health." Can this kid be real?

Certainly, the NBA hopes so. "This is a league that needs someone to be a positive force for it," says former Miller Brewing Co. marketing executive Rick Burton, director of the Warsaw Sports Marketing Center at the University of Oregon. "Kobe Bryant has all the tools to do just that."

"REFRESHING." That's why the NBA and NBC Inc., which owns pro basketball's national broadcast rights, were quick to put Bryant before the cameras at February's All-Star Game. It's also why companies are lining up to throw money at him. Like Jordan, Bryant has his own shoe, the KBs, which Adidas sells for \$100 a pair, as well as endorsement contracts with Spalding and Sprite. In all, this year those deals could add an estimated \$5 million to his \$1.2 million annual salary. A deal with a fast-food company, said to be McDonald's, has been in negotiations for months. And more are only a telephone call away. "He's one of the few guys who could get with-in shouting distance of the \$40 million or more [in marketing deals] that Jordan gets," says Burton. Adds the NBA's Welts: "He projects values not just in sports but in American life that people find refreshing. Combine that with what is obviously huge raw talent...and the sky's the limit."

But all that cash could be chump change compared with the contract that Kobe could negotiate when he becomes a free agent in 1999. Bryant's former agent, Rick Bradley of the William Morris Agency, figures that Kobe can pull in



A SEASON TO FORGET?

So far, 1997-98 has been one headache after another for the NBA

- ▶ Jordan's musing about retiring from basketball gets louder.
- ▶ Latrell Sprewell's \$24 million contract with the Golden State Warriors is terminated. He is suspended for one year for attacking his coach.
- ▶ Washington Wizard Chris Webber gets busted for possession of marijuana.
- ▶ Kenny Anderson refuses to report to Toronto, forcing the Raptors to ship him to the Celtics.
- ▶ Miami Heat forward Keith Askins is suspended for two games and fined \$10,000 for slamming New Jersey Net Keith Van Horn.

the sort of \$100 million-plus, multiyear deal that the Timberwolves gave Kevin Garnett.

Of course, as Welts notes, first you have to win championships to be regarded as a real superstar. "What Kobe is," says Lakers coach Del Harris, who spent last summer working with Bryant, "is a bundle of potential. You can't have one hit song and be compared with Frank Sinatra. Greatness comes with consistency over time."

Right, and you've got to be able to handle the heat. Marketers have showered money on young stars before, only

to see them wilt under the expectations that accompany the cash. Even now two years after the Lakers made center O'Neal one of the game's wealthiest players, there are rumblings that his game has been undermined by endorsements and the lure of film and record deals. But Kobe is no fool. "I definitely don't want to overextend myself," he says. "People can become bored with you. 'Oh, him again. I see him all day all the time.' From a business aspect that's important."

Indeed, from the beginning, the game plan Bryant's advisers put together, says Bradley of William Morris, was "to go slow so that his game can develop." These days, the management of Kobe is largely a family affair. Although the brain trust is headed by Los Angeles sports

BRUISES

Sprewell brought the issue of racial tension in the league to the fore

lawyer Arn H. Tellem—who also represents Sprewell—Team Kobe is run largely from the Pacific Palisades mansion that Bryant rents and that houses his family. Most of the deals are approved by his father

Joe "Jellybean" Bryant, a former pro player. Joe taught Kobe the game as the family traveled from team to team together, ending up in Italy for the last seasons of a checkered career.

It wasn't until the Bryants relocated to Philadelphia that the buzz about Kobe began. He was named *USA Today's* player of the year in 1996, the year he led Lower Merion High School to the Pennsylvania state championship by averaging 31 points and 12 rebounds a game. A better-than-average student, he scored an impressive 1,100 on his SATS (out of a maximum 1,600), though he made the controversial decision to forgo college. The Charlotte Hornets selected him in the 13th round of the 1996 draft and then traded him to the Lakers.

At only midway through his second season, Bryant seems firmly on his way to basketball's top tier. His current scoring average of 17 points a game ranks 29th in the league, though he is a non-starting reserve who plays just over half a game. Those numbers feed the inevitable comparisons with Michael Jordan. "It's cool. It's very complimentary," says Bryant. "If it happens, it happens." If it doesn't, Kobe Bryant will always be the man who could have been king.

By Ronald Grover in Los Angeles with Mark Hyman and Ciro Scotti in New York

Portfolio enhanced, earnings higher

- **Result of ordinary activities up 70% to \$ 0.95 bn**
- **Higher dividend**
- **Order intake increased by 16%**

Mannesmann boosted its result of ordinary activities in 1997 by 70% to \$ 0.95 bn. All four sectors, Engineering, Automotive, Telecommunications and Tubes & Trading, posted higher earnings.



The net profit for the year of around \$ 334.8 m is on a par with that of the previous year. Due to the decline in minority interests, the share of the net profit for the year attributable to Mannesmann shareholders has risen. Mannesmann intends to increase its dividend to \$ 5.60 per share. This is the fourth dividend increase in succession.

Order intake and sales increased, very high level of investment
Orders received climbed 16% in 1997

to \$ 23.1 bn, while sales rose by 13% to \$ 18 bn. All sectors contributed to this improvement. At the end of 1997, Mannesmann had approx. 120,400 employees (+1%). Investments reached a very high level, above all due to major projects in Telecommunications.

Portfolio enhanced

Mannesmann again greatly strengthened and enhanced its product portfolio in 1997. In Engineering the bundling of our plastics machinery activities in Mannesmann Plastics Machinery went into effect at the beginning of 1998. We hold a leading position worldwide in this field.

In Automotive the acquisition of Philips Car Systems will greatly increase the competence of VDO and enable it to cover a broader segment of the market. Sachs has largely completed its process of optimization and is now focusing on its core business of supplying automotive components.

In Telecommunications the focus of attention was the acquisition of a stake in OliMan (Italy) and Cegetel (France). These measures will significantly strengthen Mannesmann's position in the European telecommunications market.

mannesmann

engineering

automotive

telecommunications

tubes & trading

In Tubes & Trading a major decision aimed at securing the future development of the sector was taken with the formation of a joint venture with Vallourec for hot-rolled seamless tubes. Vallourec & Mannesmann Tubes is the top international player in its field.

Details are contained in our Shareholders' Newsletter, which we will be glad to send to you on request.

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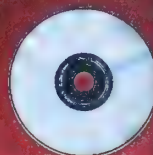
Group performance		Jan-Dec 1997	Jan-Dec 1996	Change abs.	%
Orders received	\$m	23,124	19,925	3,199	16
External sales	\$m	21,783	19,353	2,430	13
Domestic business	\$m	9,648	8,392	1,296	15
Foreign business	\$m	12,135	10,961	1,174	11
Employees (31.12.)		120,380	119,709	671	1
Investments	\$m	4,862	1,999	2,863	143

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LOCKED OUT OF THE HOSPITAL

medical buying consortiums squelching innovation?

1993, Dallas engineer Thomas J. Shaw and his colleagues came up with a striking innovation. They designed a hypodermic syringe that promised to slash the incidence of accidental needle sticks, which each year cause about 640,000 injuries among health-care workers. Safety-conscious hospitals, he figured, surely would sign up to his fledgling Retractable Technologies Inc., a newly held outfit in Little Rock, Tex.

He was wrong. In fact, he says now, his salespeople can't even get inside many U.S. hospitals to demonstrate their syringes and blood-collection devices. "Thousands of hospitals are obliged to buy from big suppliers that have negotiating-term, multibillion-dollar contracts with Premier Inc. and VHA Inc.'s subsidiaries, two of the nation's largest health-care group purchasing organizations (GPOs). Smaller companies, like Retractable, are effectively locked out."

KEHOLD. GPOs, which help hospitals save millions of dollars on medical supplies by buying in bulk, have thrived for decades. In the past few years, though, these for-profit companies, typically owned by member hospitals, have consolidated rapidly into hugely powerful buying consortiums. The six largest GPOs administer contracts for at least half of the nation's approximately 5,400 health-care hospitals. That adds up to about \$25 billion of supplies, according to the Marketing Group in Chicago. San Francisco-based Premier, created by a three-company merger in January, 1996, alone is buying for about a third of U.S. hospitals. Novation was formed in Janu-

ary '98 when VHA and University HealthSystem Consortium merged their supply operations.

Boosters claim that GPOs have saved hospitals about 5% of spending on commodity products and over 25% for high-tech equipment—a godsend for institutions battling declining reimbursements from insurers and escalating prices. Yet critics argue that these big consortiums, by removing purchasing decisions from clinicians and discouraging product innovation, may in fact be jeopardizing quality and safety and putting medical

professionals and patients at risk. GPOs are "making it more difficult for small companies to get their products into the marketplace," says Dr. Janine Jagger, director of the University of Virginia's International Health Care Worker Safety Center. Market concentration, she adds, is "not good for the safety field."

STIFF RULES. GPOs squeeze out savings for hospitals by negotiating hundreds of exclusive deals with medical-gear and supply vendors for a broad array of products. To qualify for discounts, member hospitals typically must buy a minimum portion of their supplies from GPO-contracted vendors. In the past two years, that portion has risen to as high as 95%. If they buy from more than a few nonapproved vendors, the hospitals lose the discount and can face ejection from the consortium.

Retractable Technologies charges that such practices amount to exclusionary restraint of trade. Aided by

"NO THANKS" TO SAFETY?

Most U.S. hospitals won't use Retractable Tech-

nologies' safer syringe (top) and blood collector (bottom) because of long-term supplier contracts

Representative Dick Armey (R-Tex.), it has complained to the Federal Trade Commission about Premier's and VHA's relationships with Becton Dickinson & Co. and Sherwood Davis & Geck, the market leaders in syringes. The FTC confirms that the case is under review.

GPOs say such scrutiny is unwarranted. "The process is quite fair both to



[suppliers] and to health-care organizations that use our group contracts," says Pat Poston, a Premier senior vice-president. Says VHA's John M. Burks, vice-president for contract services: "We're customer-driven. If the customer told us they wanted this stuff, we would be stupid not to get it on contract." Special clauses in contracts preserve VHA's right to buy new technology, he says.

Retractable isn't alone in complaining that it's locked out by GPOs. Remel Inc., a Lenexa (Kan.) unit of Sybron International that makes culture mediums used for identifying various bacteria, has already been dropped by some 200 Premier-supplied hospitals in favor of Becton Dickinson products, and more hospitals are under orders to do so by Apr. 1—even though the Food & Drug Administration, in a Dec. 16 letter, admonished the Becton unit for poor quality control.

In fact, when defective batches of Becton's chocolate agar—used to test for deadly meningitis bacteria—showed up in hospital labs last year, some hospitals that depended on the product had to scramble for emergency supplies, says Dr. Alice S. Weissfeld, president

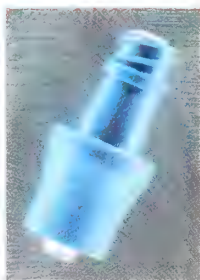
CONTRACT HELL

A product from Becton keeps Bio-Plexus' Punctur-Guard blood collection needle out

of Microbiology Specialists Inc., a Houston diagnostic lab. "The potential for something horrible to happen was certainly there,"

she says. Becton says it has solved the quality problem; a Premier spokesperson says: "We followed up with Becton Dickinson and the hospitals to see that the appropriate actions were taken."

Another product apparently stymied by the GPOs: a needleless intravenous system made by ICU Medical Inc. in San Clemente, Calif. After Premier negotiated a \$7 billion, seven-year contract with giant Baxter International Inc. in 1996, member hospitals were under pressure to buy Baxter's competing IV. That irked the infection-control director at one Louisiana hospital, where the ICU device was found to be safer, more convenient, and more patient-friendly. "I just question whether bigger is always better," she says. Bio-Plexus Inc.'s blood-collection device also competes head to



SEVEN-YEAR HITCH

Premier's pact with Baxter means its hospitals won't use ICU's needleless intravenous connector

head with a Becton product, and it, too, has seen its prospects sour. The long-term contracts make it tough to "try to make a brand out of an idea," says Bio-Plexus marketing chief Thomas K. Sutton.

Like Remel, ICU Medical, and Bio-Plexus, Retractable appears to offer a product with distinct advantages. Inspired by a news report Shaw saw in the late 1980s of a physician who accidentally stuck himself, the VanishPoint's spring-loaded needle collapses back into the syringe chamber after an injection. The syringe, developed with funding from the National Institutes of Health, won FDA approval and enthusiastic receptions at trade shows. "We examined all known products and found this to be the best. It's technologically superb," says Dr. Leslie M. Beitsch, assistant secretary at the Florida Health Dept., where RTI syringes are being used at more than 100 public health facilities.

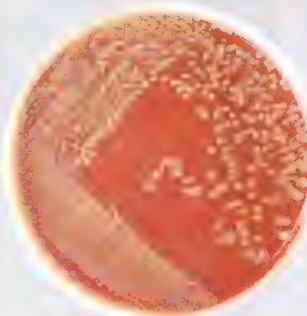
Retractable's outlook seemed bright—but its timing proved terrible. In December, 1996, Premier Inc. announced a \$1.8 billion, 7½-year supply contract with Becton Dickinson. Suddenly, every Premier hospital—including some of Retractable's hottest prospects—essentially was required to buy Becton's syringes. Some hospitals affiliated with Premier and VHA, which had been buy-

ing from Sherwood for nine years, declined to consider Retractable's VanishPoint syringe at all.

One of those was Shannon Medical Center in San Angelo, Tex., which stands to lose "incentive payments" of more than \$100,000 a year if it fails to buy 95% of its products under 13 different VHA contracts. "Sherwood offers a shielded syringe that, as far as I'm concerned, is a competitive product," says Carolyn Tegeler, Shannon's director of materials management. But she admits that the medical center's nurses who tried Sherwood's safety syringes "felt as if they caused needlesticks," so they aren't using them. If Retractable's product had been under VHA contract, she says, "we might have come closer to looking at it."

Some hospitals that decline to buy Retractable's syringe cite its price of

about 50¢ per unit, more than double that of competing products. But because the use of Retractable's Vanish-



UNEARNED BUSINESS

Agar maker Remel lost buyers to a Becton unit cited by the FDA for poor quality control

Point results in lower disposal costs and lower workers' compensation insurance premiums, the overall cost is less, says Sally Peerbolt, an employee-health nurse at Riverside County Regional Medical Center in Riverside, Calif., a Retractable customer. And using Retractable's syringe, she adds, "cuts down on anxiety and stress" among health-care workers.

Rather than trying to break into the GPO game, Retractable retreated, focusing on public facilities, including veterans' and prison hospitals, about a 10% slice of the market. In 1997, Retractable sold about a half-million units, generating \$250,000 in revenues but no profits, Shaw says.

Shaw is pinning his hopes largely on regulatory, legal, and legislative relief. Those remedies may win Retractable broader access to hospital contracts. But it's not clear that they will address the bigger question about group-purchasing organizations—whether they constitute a system of exclusive long-term contracts that reduces hospitals' costs at the risk of stifling medical innovation and impairing patient care.

By Phillip L. Zweig in New York and Wendy Zellner in Little Elm, Tex.

THE QUIET HOSPITAL GIANTS

Leading hospital group-purchasing organizations (GPOs) and the number of hospitals they supply

GROUP	ACUTE-CARE HOSPITALS**
PREMIER INC.	1,682
AMERINET	1,493
NOVATION*	1,400
MEDECON SERVICES	770
HEALTH SERVICES CORP.	679
JOINT PURCHASING CORP.	382

* Jointly owned by VHA Inc. and University HealthSystems

** Some hospitals have contracts with more than one GPO

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THE HEAT UNDER PETER KNIGHT

A Gore confidant is at the center of the Portals probe

As Vice-President Al Gore contemplates the White House, Hill Republicans are trying to tie him to a white elephant—the Portals, an office site in a forlorn corner of Washington that has been the object of a 10-year struggle between congressional committees, the Federal Communications Commission, and developers. The Justice Dept. and Congress are investi-

gating whether Tennessee developer Franklin L. Haney, a longtime Gore pal, made sizable campaign contributions to Democrats in return for favorable lease terms on the Portals. And now, one of Gore's closest associates has been drawn into the inquiry.

Investigators want to know whether Haney violated federal laws when he paid \$1 million to Peter S. Knight, a Gore confidant and head of the '96 Clinton-Gore Reelection Committee, alleged-

ly for interceding with government officials to win changes to the Portals lease that benefited Haney financially. A Haney spokesman says Haney paid the \$1 million but that it was not just for Portals work. The spokesman adds that Haney's \$230,000 in 1996 contributions were "handled according to appropriate laws and regulations."

The House Commerce Committee, which oversees the FCC, began its own probe after a previous BUSINESS WEEK story (BW—Oct. 13, 1997). Says Committee Chairman Tom Bliley (R-Va.): "I am puzzled by public statements of Franklin Haney, Peter Knight, and the FCC, which do not correspond fully with some of the key facts we have uncovered." Meanwhile, as Congress and the FCC continue to wrangle over the move to the Portals, taxpayers are paying rent on an empty building—to the tune of \$9 million so far.

Knight's involvement in the Portals project dates back to the summer of 1994, when he recommended old friend

THE PORTALS AFFAIR KEEPS UNFOLDING

■ **AUGUST 1994** A U.S. appeals court rules that the GSA must honor a commitment to lease a not-yet-built office building (Portals II) in an isolated pocket of southwest Washington. The GSA quickly signs a lease with Portals developers.



KNIGHT

■ **SEPTEMBER 1994** On the recommendation of ex-Gore aide Peter Knight, FCC Chairman Reed Hundt hires Robert A. Peck as a deputy. Peck volunteers to take over the FCC's move to the Portals.

■ **MAY 1995** Knight asks

Peck to meet with Franklin L. Haney, a home-state friend of Gore and major real estate developer. Haney is considering an investment in the Portals project.

■ **JUNE 1995** Haney attends a fund-raising dinner, coordinated by Knight, at Gore's residence.

■ **JULY OR AUGUST 1995** The FCC's Peck meets with Haney at Knight's office. No official record of the meeting exists since it took place off FCC premises.

■ **AUGUST 1995** Knight arranges for

Haney to meet with GSA officials to discuss lease modifications so Haney can finance the Portals project with tax-exempt bonds.

■ **OCTOBER 1995** Knight sets up a third meeting, this time in the office of FCC Chairman Hundt, whose calendar shows Peck, Knight, and Haney in attendance.

■ **NOVEMBER 1995** The GSA again formally assigns the FCC to the Portals, a move that surprises many, considering that the FCC had rejected the Portals space earlier that year and was seeking independent leasing authority from Congress.

■ **DECEMBER 1995** Peck, again with Knight's help, leaves the FCC for the GSA, where he oversees all government office leasing.

■ **JANUARY 1996** The GSA and Portals developers sign a supplemental lease with terms advantageous to Haney's bond issue.



GORE

The lease language stipulates the FCC as the tenant and a firm start date of July, 1997, for rental payments. On the same day, Knight bills Haney \$1 million for "legal services rendered (1994 and 1995)."

■ **MAY 1996** Knight is named chairman of Clinton/Gore Reelection Committee. Haney contributes \$230,000 to the DNC and five state Democratic parties two weeks after the Portals bond sale.

■ **FEBRUARY 1998** The General Accounting Office issues a study saying the FCC move to the Portals is in the government's best interest.

■ **MARCH 1998** The FCC continues to balk at the Portals move, citing safety concerns because of its remote location. Total rent paid on the empty building so far: \$9 million.

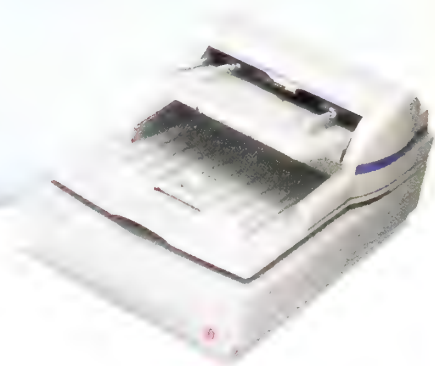
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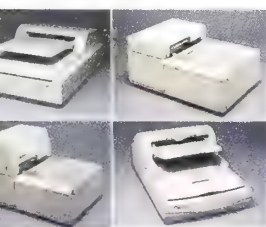
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Robert A. Peck for a job as deputy to then-FCC Chairman Reed E. Hundt. A year later, when Haney, one of Knight's law-firm clients, was deciding whether to help bail out the floundering Portals project, Knight turned to Peck for help in arranging meetings for Haney.

After a year at the FCC, Peck told Knight he wanted a new job. Knight recommended him to the General Services Administration, where he now oversees all government leases, including the FCC's. Peck says in both cases his credentials as a real estate lawyer and legislative aide won him the government jobs, not Knight's assistance.

WEB OF CONTACTS. Knight, Peck, and Haney all deny wrongdoing and point to a Feb. 27 General Accounting Office study as vindication. The study concludes that it is in the government's best interest that the FCC move its headquarters to the Portals. And it says that the GSA followed federal procurement rules in selecting the Portals in the first place. But the study also says it did not assess allegations that the GSA's decisions were unduly influenced because those were "not included within the scope of our review." Haney's spokesman says that the developer met with top officials to gather information needed to take the project to the bond market, and that in doing so, he followed all necessary federal procurement rules. He adds that Haney is not a target of a Justice Dept. investigation. "Mr. Haney did not request or receive any favors or interventions in this transaction from Vice-President Gore or his office," says spokesman Kenneth Vest.

This Washington world where business and politics intersect is one that Peter Knight knows well. A former Gore staff chief who ran his boss's failed '88 Presidential bid and his successful '92 Vice-Presidential campaign, Knight personally placed hundreds of job-seekers in sub-Cabinet posts during the transition period before Clinton took office. In mid-1993, he returned to private law practice at what is now Wunder, Knight, Levine, Thelen & Forsey. Except for a brief interruption in 1996 as manager of the Clinton-Gore campaign, he has remained at the firm, where he counts Bell Atlantic Corp. and Lockheed Martin Corp. among his clients. But Knight has continued to advise agencies seeking to fill high-level jobs. That has helped him build a vast network of contacts.

In 1995, Haney, a Chattanooga developer who once worked in the Senate office of Al Gore Sr., retained Knight for the Portals project. Haney had been in-

involved in numerous government real estate deals and was known as a master of selling tax-exempt bonds, backed by government rent payments, to finance his projects. Knight's job: help Haney refinance the Portals complex using tax-exempt municipal bonds.

When he jumped into the Portals deal, Haney found the FCC development bogged down after years of Washington infighting between Congress and the FCC. FCC officials opposed moving to what they considered a barren area in Southwest Washington cut off from



HUNDT

During his tenure as FCC chairman, Hundt says he was caught in the congressional crossfire over whether to move the agency to the Portals

restaurants and shops. But to the project's owners, landing the FCC was crucial: They needed the agency to serve as a magnet for telecom law firms, consultants, and lobbyists who would fill three other planned buildings in the complex.

Knight arranged for Peck, who had taken over the Portals project soon after arriving at the FCC, to meet with Haney at Knight's office. Sources say they discussed the FCC intentions about the Portals move. This contradicts earlier statements made to BUSINESS WEEK by the GSA, the FCC, and Haney spokesmen, all of whom maintained that, by the time of Haney's involvement, the FCC's move was a fait accompli. Peck, however, now concedes "there were lots of questions people [including Haney] had about the project. If a project depended on a particular tenant, I would think you'd do everything you could to make sure that that tenant moved in." He strongly denies that he or anyone else did any favors for Haney.

Next, Knight had to persuade the GSA to make key changes in the Portals lease that had been signed before Haney's involvement. Knight arranged for Haney to meet top GSA officials in August, 1995.

According to one source at the meeting, Haney's changes included a firm startup date for rental payments, which he needed so he could presell bonds and use the proceeds to finance the project. Documents reviewed by BUSINESS WEEK show that the GSA career staff had serious reservations about granting a fixed date to begin paying rent because of the project's tortuous history.

In October, 1995, Knight arranged a third meeting, this time between Haney and Hundt in the FCC chairman's office. Hundt says he can't recall whether

Haney was there that day but remembers meeting former Tennessee Senator and now U.S. Ambassador to China James R. Sasser, who brought "someone else." Sasser represented Haney at the time. Peck also was present. Hundt months ago said he recalled first meeting Haney in late 1996 to discuss changes to the building. In November, 1995, the GSA formally assigned the FCC to the Portals building, a move that surprised many telecom lawyers and FCC staff closely watching events.

"SERVICES RENDERED." Knight's work came to fruition on Jan. 3, 1996, when the Portals partners and the GSA signed a new lease with several key changes, the most significant of which was the

July, 1997, startup date for rent payments. Because of that clause, the GSA has had to pay \$9 million to date for an empty building. It will have paid a total of \$15.7 million by August, when the FCC is scheduled to move in.

On the same day as the lease signing Knight signed a \$1 million bill sent to Haney for "legal services rendered" in 1994 and 1995. Haney's spokesman says the money covered Knight's "strategic and legal counsel" for three years on a dozen projects besides the Portals deal but declines to name any of the others. An October, 1995, letter of engagement signed by Haney and Knight refers to legal work Knight will perform, back dated to June 1, 1995, but no reference is made to work done in 1994. Knight declined to comment on the bill because of the investigation.

Federal law forbids the payment of contingency fees on government contracts. But Haney's spokesman denies that the fee was contingent on the signing of a new lease. So why was the \$1 million invoice written on the same day as the lease signing? Just a coincidence, says Haney's spokesman.

By Paula Dwyer in Washington



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WHAT THE HECK IS GOING ON AT REUTERS?

Suppliers claim the media giant copies proprietary software. It all may end up in court

Reuters vs. Bloomberg. The two behemoths that dominate the rapidly growing financial-information business have long been archrivals. The depth of that rivalry became apparent in late January, when Reuters Group PLC disclosed that a subsidiary was the subject of a grand jury investigation in New York for improperly obtaining and using information from Bloomberg LP.

Now, Reuters stands accused of additional questionable behavior—in particular, taking proprietary ideas and software applications from rivals and partners both in the U.S. and Europe. **BUSINESS WEEK** canvassed many of the approximately two dozen software vendors who have worked most closely with Reuters developing specialized software to analyze financial data.

BOLD STEPS. While a few spoke well of Reuters, executives at nine software houses recalled instances where they thought software or information was improperly copied by the \$4.7 billion-in-sales company. Those executives depict a company that sometimes allegedly uses dubious business practices and strong-arm legal tactics. And they tell of an intimidating corporate culture in which Reuters officials are quick to threaten vendors with legal action. At least two of these vendors say they may file civil-racketeering suits against Reuters, alleging a pattern of abusive behavior.

Peter Job, CEO of Reuters Group, and Michael O. Sanderson, CEO of Reuters America Holdings Inc., declined comment. But Robert Crooke, vice-president for media relations at Reuters America, says: "We have largely good relations with [vendors], barring the occasional squabble and, even more rarely, legal disputes, which are typical in any business."

Reuters' reliance on outside vendors, explain industry executives, stems from the company's weakness in developing its own software. Such programs help Reuters' clients with tasks like analyzing market risks and iden-

“They try to intimidate you until you give up your rights on the contract”

—MILAN SULC

*CEO of Typlan,
a software company*

“I would never enter into a relationship with Reuters again.

I think they are unethical and heavy-handed”

—PETER DAVIES

*Former senior-level consultant
to Reuters; founder of Sailfish*

“Reuters has ruthlessly exploited its dominant position...to maintain its pricing policies and to limit competition. [It] has practiced various forms of abuses globally”

—GERALD SHARROCK

Former Reuters in-house counsel

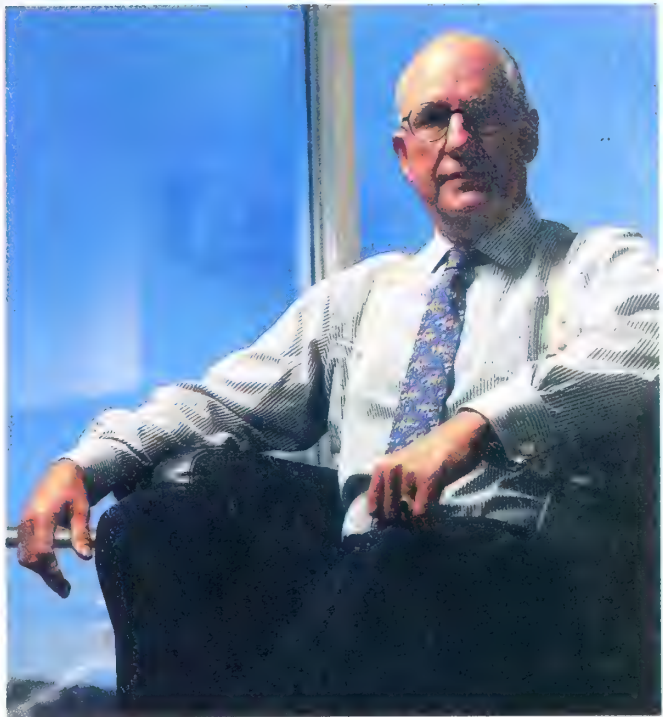
tifying historical bond spreads.

Among vendors critical of Reuters is J. Stephen Levkoff, founder of Capital Market Decisions, which sued Reuters in 1993 for breach of contract and unfair business practices. "I was the first person to stand up and say Reuters is trying to steal my business," Levkoff says. In affidavits, Levkoff said Reuters executives tried to clone his analytical software product, Decision 2000, which was built to be a direct competitor to Bloomberg. He said the reason was to avoid paying him royalties. The case was settled out of court, and Reuters later bought the company for an undisclosed sum. "Given the Bloomberg situation, we feel very vindicated," Levkoff says. Crooke says it is "inappropriate...for either side to be commenting in public since it has been apparently resolved."

"Our experiences were eerily similar" to Levkoff's, says Peter Davies, a former senior-level consultant to Reuters and founder of Sailfish Systems, a New York financial software company. Davies says he entered into a joint marketing agreement with Reuters, which promised future revenues and marketing support. But nothing materialized, leaving Sailfish financially overextended. Davies felt forced to accept Reuters' lowball offer to buy Sailfish. Davies claims Reuters said: "We don't need you. We could develop the same product internally anyway." Says Davies, "I would never enter into a relationship with Reuters again. I think they are unethical and heavy-handed."

Responds Crooke: "We believe we have acted fairly and ethically in our dealings with Peter Davies and that Mr. Davies benefited substantially from his association with Reuters."

Milan Sulc, CEO of Typlan, a Swiss software company based in Bern, is also unhappy with Reuters: "They try to intimidate you until you give up your rights on the contract," he says. Sulc alleges that Reuters illegally installed \$2 million to \$6 million worth of Typlan software last year and failed to pay an-



RED FIRE: Job and Sanderson head a corporate culture that rivals and vendors say is often intimidating

inform Typlan. Reuters said on 3 that it was conducting an inter-adit into possible unlicensed use plan software in its European news tions. Says Crooke: "If monies are Reuters will fulfill its obligations its agreements with Typlan."

OWING? Another software exec of being invited to Reuters head- ers a few years ago to display ew software. After the demo, ers execs took the entrepreneur ch. When they returned, he says, Reuters computer, with the ven- software inside, was gone. "We told it was taken to another demo for another client," says the exec, asked not to be named. "They 'Thanks for the demo, we'll be in touch with you.' No deal was done with us. And we never got software back." He says he later elements of his software incorpo- in Reuters programs: "There's estion that they've been borrow- ur designs. No question whatso- ' Reuters officials deny any such ent took place.

Reuters executives insist that soft- companies that complain about ers are disgruntled over deals that n't as lucrative as they planned. ers even offered BUSINESS WEEK a f vendors for references. Andy director of business development Market Arts Software, a New York are and consulting company, says: ters' dealings with us have been mely beneficial for both parties." t BUSINESS WEEK had previously

talked to one company on the Reuters' list that complained of "being a victim of Reuters' policy of checking out every- body else's ideas. Whatever is good, they absorb for their own use. Then they leave you with a much weaker place in the market. They absorbed all our features into their own offering."

Most of these complaints are support- ed by Gerald Sharrock, a former Reuters

“We have largely good relations with [vendors], barring the occasional squabble.”

— ROBERT CROOKE

Vice-president for media relations, Reuters America

in-house lawyer. "Reuters has ruthlessly exploited its dominant position in finan- cial-information markets to maintain its pricing policies and to limit competition," says Sharrock, who left Reuters in 1993 for health reasons. "Reuters has prac- ticed various forms of abuses globally...[including] misusing vendors' pro- prietary information and developing it in-house." Sharrock, who has detailed knowledge of how Reuters operates, could prove to be a major headache. He is now a consultant who offers legal and technical advice to software houses that work with financial-service companies, including Typlan.

Sharrock says he has observed Reuters' behavior with small, innova- tive software houses. First, he says, Reuters woos the vendor with offers of global deals, such as joint marketing agreements. Typically, Reuters gives the vendor a long list of software changes that must be made before Reuters will release the product. While the company is making the changes, which can take 18 months to two years, "other parts of Reuters are negotiating to make a similar product either internally or with other software houses," says Sharrock. Along the way, he adds, Reuters gets access to vendors' confidential designs and uses them to make its own prod- ucts. Plus, "Reuters doesn't hesitate to make frequent use of their powerful legal department to ensure that software houses cave in to their demands," Shar- rock says.

Crooke says information Sharrock may have received during his Reuters employment is confidential: "He had no right to disclose this information.... In the circumstances, therefore, we cannot comment on whether his claim is true or false." Says Sharrock: "There was no need to use confidential information in the conclusions I arrived at."

All of these disputes boil down to one issue: how information is used. There is often a fine line between legiti- mately building on the work of others and improperly taking it without com- pensation. The question is whether in dealing with software vendors Reuters crossed that line.

By Debra Sparks in New York

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THE DEALMAKER

1982 Farkas joins a startup real estate syndication group. In 1983, launches his own real estate investment banking group. Syndicates real estate limited partnerships.

1986-88 Partnerships unravel. Pursues a leveraged buy-out and other deals.

1989-91 Raises \$5.5 million to acquire control of distressed real estate limited partnerships. Takes company public in 1993 and starts on acquisition trail.

1996 Acquires commercial real estate brokerage firm Edward S. Gordon Co.

1997 Purchases 10th-largest single-family-home brokerage business. Plans a real estate investment trust for apartment holdings.

1998 Acquires Richard Ellis Group, a leading property manager in Britain. Pursues further U.S. and European transactions.

DATA: BUSINESS WEEK



ANDREW FARKAS: "We are the quintessential public real estate opportunity fund"

REAL ESTATE

THE MAKING OF A SUPERLANDLORD

Insignia aims to be a one-stop shop for real estate services

In 1988, 27-year-old Andrew L. Farkas saw his budding business—syndication of real estate limited partnerships—crash and burn. His investors, including friends and family, took big financial hits, and Farkas came close to personal bankruptcy. Fast-forward 10 years. Farkas now heads up Insignia Financial Group Inc., a rapidly growing, highly acquisitive real estate services firm with a market capitalization of \$700 million. After just eight years in business, Insignia is the largest manager of apartment housing in the U.S., has real estate holdings of \$250 million, is a leading firm in commercial brokerage, and is

among the top 10 residential brokers. Now, it is expanding overseas.

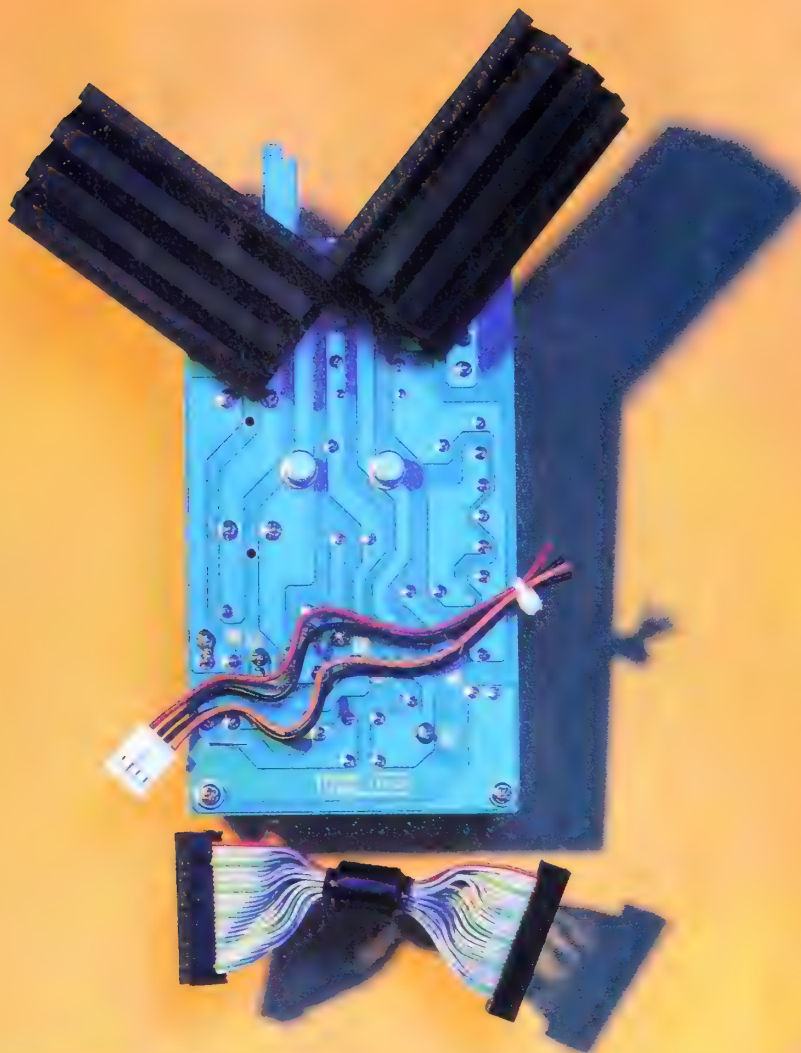
Farkas' success is, to some degree, an outgrowth of his earlier failure. By launching—and then trying to salvage—real estate limited partnerships, Farkas hit upon a novel way to capitalize on ailing partnerships. By buying a controlling interest in a limited partnership (LP), Farkas, as general partner, could assign the management contract to his property-management company.

This laid the foundation for his current strategy. Farkas is now set on becoming the leader in a fast-consolidating real estate services industry. "Insignia is very,

very aggressive," says Michael L. Evans, national director of E&Y Kenneth Leventhal Real Estate Group. "Farkas only started his business in the late 1980s, and he has now become the 800-pound gorilla."

Farkas faces formidable challenges. He is competing with well-established players, including Los Angeles' CB Commercial and Chicago's LaSalle Partners Inc. While competing for clients and choice acquisitions, Farkas must manage the staggering growth of his company. He must also contend with some unhappy limited partners who allege that, in connection with a series of tender offers that Insignia began making to LPs in late 1994, the firm, as the LP's general partner is shirking its fiduciary duty—a claim Insignia vigorously denies.

WHO'S WHO. Farkas' tenure in the industry can't compare with James J. Didion's 36 years at CB Commercial, where Didion is now chairman. CB Commercial is also pursuing a goal to become a one-stop shop for real estate services. But Farkas brings a wealth of connections to the table. His grandfather founded the now defunct Alexander's department store chain, and he grew up in the same



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New York apartment building as vulture investor Leon Black. Now, Black's company, Apollo Real Estate, owns a large slice of Insignia and invests in many of the firm's deals. Farkas and William Lauder, of the cosmetics empire, are part of a group of friends that are a Who's Who of moguls-in-the-making. The circle includes Strauss Zelnick, president of media giant Bertelsmann's U.S. operations; Michael Lynton, Penguin Group chief executive officer; and Seagram heir Matthew Bronfman.

Farkas describes his firm as "the quintessential public real estate opportunity fund." Part of its strategy is to invest alongside the institutional owners it provides management services for. Once it finds properties it thinks its clients would like, Insignia goes to clients with the deal, asking to co-invest by injecting 10% to 35% of the equity and to manage and lease the entire property. Insignia gets a brokerage fee, too. Farkas says the firm has "tens of millions" co-invested in assets with gross valuations of about \$1 billion.

Farkas' vision is of a real estate supermarket serving residential and corporate customers around the U.S. He sees synergies between, say, his mortgage-banking business and his single-family-home brokerage arm, which could work when tenants depart to buy their own houses. His desire to buy strong firms in consolidating industries led to purchasing single-family residential brokerage firm Realty One in Cleveland last year. It is the first step in Farkas' plans to create a national independent network of residential brokers.

POWERHOUSE. The deal that put Insignia on the map in the commercial real estate brokerage industry came in mid-1996, when it bought Edward S. Gordon Co. (ESG), a New York powerhouse. "Insignia hadn't really been a competitor until it acquired ESG," says Didion. "We see Insignia as a rising entity. If Farkas can integrate it all, he'll have a formidable operation." Insignia has also bought brokerage firms in Chicago, Washington, and other big cities. He is taking the Insignia/ESG name nationwide, which could diminish the value of regional brands he has acquired. (Insignia/ESG is a real estate



"We see Insignia as a rising entity. If Farkas can integrate it all, he'll have a formidable operation"

CEO JAMES DIDION OF CB COMMERCIAL

consultant for The McGraw-Hill Companies, BUSINESS WEEK's parent.)

Insignia is also advancing in its international push, although CB Commercial beat it out for London's REI Ltd., which operates in 28 countries. Insignia, however, beat out its rival for Richard Ellis Group, a leading real estate services and investment firm in Britain.

Farkas plans to merge the firm's partnership interests into a publicly traded real estate investment trust. Insignia Properties Trust (IPT), now a private REIT, is awaiting regulatory approval to go public. It will be a "paper-clipped" REIT, which trades separately but has the same management and board of directors as Insignia, which will initially own about 66% of IPT.

Insignia says that the main purpose of the REIT is to separate its real estate services and ownership businesses. Also, IPT will be able to access public markets to help fund growth. The move may bring shareholders added value. In 1997, Insignia's stock rose only 2.2%. But so far this year, the stock, at 24%, is up 6%.

IPT will be an unusual REIT. "It has a

built-in growth vehicle—the consumption of all those LPS," says Ron Sachs, a research analyst at Janus, a major holder of Insignia stock. "Insignia has been able to make incredibly attractive acquisition because they know what the properties are worth."

CONFLICTS. Such statements make some limited partners boil. Insignia has been hit with a string of lawsuits since it began making discounted tender offers in late 1994. Some lawsuits alleged that Insignia's offers were inadequate and constituted unjust enrichment. Unhappy limited partners say that Insignia, since it gets fees from properties, has a disincentive to liquidate partnerships. Insignia gets \$30 million to \$40 million in revenue a year from 5% of gross rents it earns as manager of its 250,000 units about half of which are owned in LPS.

Insignia lays out the conflict for limited partners. A recent offer states: "The General Partner has conflicts of interest...including the fact that a sale or liquidation of the...Partnership's asset would result in a decrease or elimination of fees paid to the General Partner," and that increased ownership by the Purchaser "...may result in a conflict for the GP in attempting to reconcile the interests of the Purchaser...with the interests of the other Limited Partners."

Insignia makes offer below what it believes is liquidation value. Says Farkas: "If we think liquidation value is \$1, we offer 65¢, and we tell the limited partner that." It's a great arbitrage for Insignia because "that 65¢ is actually worth \$1.30 because of the way REITs are valued in the market today—at a premium."

Farkas, usually animated, grows even more so when questioned about the lawsuits from limited partners. "If we hadn't come along to save these partnerships, the vast majority of them would be in bankruptcy or gone," he says, adding that lawsuits are inevitable with tender offers. "We've filed 50 tender offers. Every single case has been dismissed or settled for a nominal sum." That's not accurate. In one suit, settled in 1995, Insignia paid tendering limited partners an additional \$6 million.

Farkas is well on the way to building his empire. But as competition for acquisitions heats up—and real estate values rise—growth will come at a higher price. Farkas has proved that he can do deals in a bull market. The real test will come when the market slows down.

By Suzanne Woolley in New York

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BEWARE THE TRADES OF MARCH

Signs point to a 'short and nasty pullback' for the stock market

Investors can rest easy on the Ides of March this year. It falls on a Sunday. But they need to be wary of days when the stock market is open. Wall Street soothsayers warn that there's trouble in the alignment of record-high stock prices, a backup in interest rates, and a slowdown in corporate profits growth (chart). All told, the March market could take back a chunk of February's gains.

That wouldn't be a disaster. After all, the Dow Jones industrial average jumped 639 points, or 8.3%, last month, the best February since 1986. By itself, the stock market's monster momentum—the Dow is up nearly 1,000 points since its Jan. 9 low—should keep prices climbing in March.

But markets that get airborne early in the year often fall back in March. Last March, the Dow dropped 4.3%; in 1994, the loss was 5.1%. "We could get a short, nasty pullback of 5% to 10%," warns John L. Manley Jr., equity strategist for Salomon Smith Barney.

The market's big gains this year come from three factors: the strength of the U.S. economy, continued low inflation, and a belief that the Asian crisis has been contained. "The IMF, [Treasury Secretary] Bob Rubin, and the bankers handled the liquidity crisis aggressively

and competently," says Charles Pradilla, investment strategist at Cowen & Co.

But that may not be the end of the story. "Now, we have to deal with the economic impact of decelerating growth in Asia," says Pradilla. The Street may get a hint of that soon, when companies that expect bad first-quarter profits start announcing the disappointments ahead of the actual earnings reports.

NOTORIOUS. Indeed, analysts have been slashing their profits forecasts for months. In early January, they predicted that profits for the companies in the Standard & Poor's 500-stock index would show a 10.4% gain over the first quarter of 1997, according to data compiled by First Call Corp. Now, the estimates have been more than halved, to 4%—and the cutting isn't over. "March is notoriously bad for earnings revisions," says Salomon's Manley. "Even if the quarter turns out all right, we're going to get a lot of bad news before we get the good."

The soft earnings might not hurt much if interest rates were still coming down. But they're not. In fact, the very resiliency of the U.S. economy that brought the market to record levels is also pushing interest rates higher. The yield on 30-year U.S. Treasury bonds bottomed out at 5.72% in early January and is now back over 6%.

Some pros worry that the winter rally made investors far too complacent about the Asian mess. Beth Cotner, who runs the Putnam Investors Fund, believes shareholders in Citicorp might be in for a rough time. The bank, which gets about half its revenue from developing markets, saw its stock fall from \$144 a share before the October crash, to \$112 in early January. But it's now just \$12 below its old high. "The peak price was set at a time when the market seemed to have no doubt about Asia," says Cotner. "Now there is plenty of doubt and many defaults to come, and the current price doesn't reflect that."

Nor have U.S. manufacturers felt the full effects of Asia's woes. The surge in exports has yet to materialize because of delays in obtaining export financing and lining up distribution. "Time will

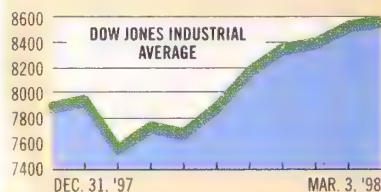


solve those issues, and then we'll see the pickup in imports and erosion in profit margins from import competition," says Greg A. Smith, investment strategist for Prudential Securities Inc. The impact may not hit until April or May, says Smith, and it could put second-quarter profits under pressure as well.

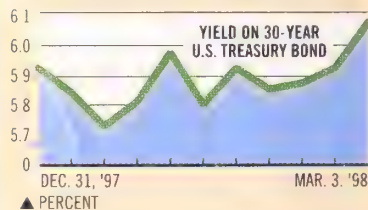
So far, none of these problems seriously threatens the long-term bull market. But with stock prices and price earnings ratios at all-time highs, the mix of higher interest rates and lower earnings does not bode well for the market's short-term health.

By Jeffrey M. Laderman in New York

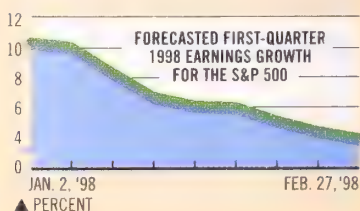
TROUBLE AHEAD? STOCKS ARE SOARING...



...BUT RATES ARE UP...

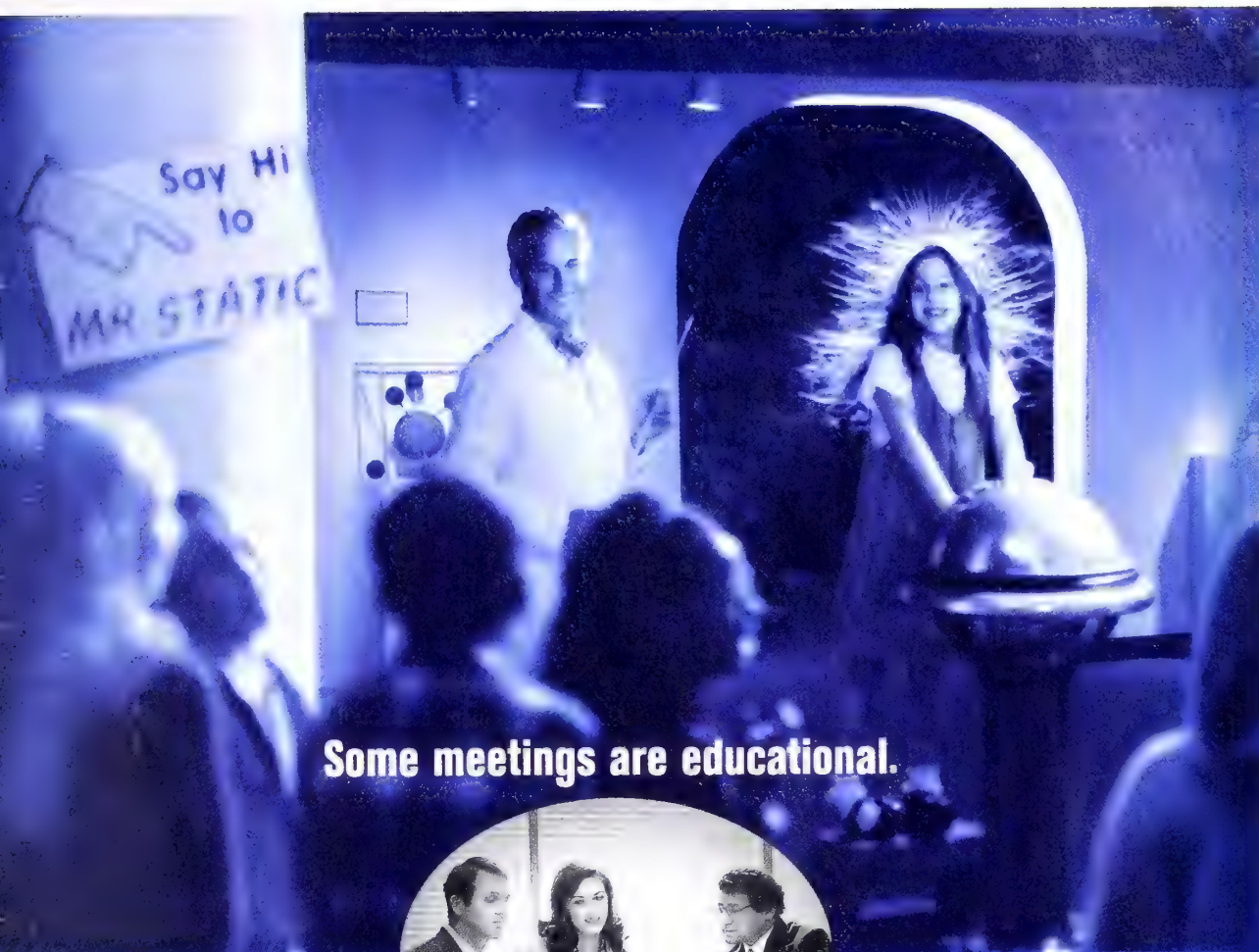


...AND PROFITS FORECASTS SAG



DATA: BLOOMBERG FINANCIAL MARKETS, FIRST CALL CORP.





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COMMENTARY

By Kathleen Morris

NOT ALL REAL ESTATE TRUSTS ARE TO BE TRUSTED

McDonald's Corp.'s latest concept for fixing its lagging stock has no ketchup, no special sauce, and no sesame seed bun. Instead, it's sort of a McREIT. The fast-food company is said to be considering selling off its huge real estate holdings—playgrounds, parking lots, even the restaurants—to a new real estate investment trust.

Most REITs focus on the business of acquiring, developing, and managing properties. But a new breed of so-called captive REITs is proliferating rapidly and raising potential problems for investors. Typically, the new REITs, in which the parent retains partial ownership, are taken public to buy the real estate holdings. "It's phase two of the REIT boom," says Lehman Brothers Inc. analyst Steven R. Hash. "Now you have nonreal estate companies trying to get real estate off the books." In the last year, companies have created REITs to hold such hard assets as prisons, car dealerships, cinema multiplexes, and golf courses. Even Walt Disney Co. has raised money by packaging some of its properties.

For McDonald's, as well as the other captive REIT sponsors, the move may not make sense. The fast food chain hasn't announced its plans. But by keeping its burgers and fries businesses but selling off its more than 12,000 restaurants, analysts estimate it could raise more than \$5 billion by selling shares to the public. That could free up capital for McDonald's to buy back shares or lower its debt.

CHEAP FINANCING. But for investors in these captive REITs, the returns may be much less palatable than expected. The cyclical recovery in the property market that has driven the boom in REIT stocks seems over. The new REITs face more limited growth due to their narrow niches. They won't necessarily benefit if their parents do well since their only source of revenue is from the leases they

hold. If McDonald's does strike gold with a new blockbuster McSandwich, the REIT won't get much of the upside. Says Fredrick Carr of Penobscot Inc., a real estate research firm that is based in Boston: "McDonald's would do a REIT because it decided it

worth of multiplexes in Nov. 18 into a new REIT, Entertainment Properties Trust. Facing a potential glut of screens, the REIT's shares are selling just below their offering price. "You're not getting the most interesting part of the action" with captive REITs, says Michael Kirby of Green Street Advisers, a REIT research firm based in Newport Beach, Calif.

So, why would someone buy shares in these captive REITs? There are pluses. With its stellar investment-grade credit, McDonald's isn't likely to default on any of its debt or leases. That means that it can, and likely will, offer shareholders a stable, high dividend of 8% or so. Against a 5.7% Treasury yield, that's attractive to some investors. But there will be little or no additional capital appreciation because growth will most likely be limited to the 2% annual increases McDonald's would likely write into them. What investors will likely get will look a lot more like a bond than the kind of REIT equities that have climbed by 20% a year or more for much of the last few years.

Conflicts of interest could also work against the growth of those dividend yields. Although the REIT and its parent are separate entities, often the same management controls both, as with Prison Realty Trust and Entertainment Properties. If management has a much larger stake in the parent than in the REIT, which is typical, it would have an incentive to favor the parent over the real estate entity. It could, for example, prevent the REIT from getting rent increases at the market rate.

All in all, for investors, many of the captive REITs are about as scrumptious as an Arch Deluxe. You're betting the management of a company you don't really own will be looking out for your interests as well.

Kathleen Morris covers real estate from Los Angeles.



Investors in captive REITs like the one McDonald's may spin off face limited growth

is cheaper financing than it can get elsewhere, not because it wants the REIT to grow."

It might be different if McDonald's were in a growth industry, like prison construction. The stock price for CCA Prison Realty Trust has doubled since its IPO last spring. But the REIT is still merely a financing vehicle for its parent, the Corrections Corp. of America. Others, such as REITs created from new car dealerships, face less certain futures. Take the AMC Entertainment Inc. theater chain that spun off \$270 million

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BY GENE G. MARCIAL

MICROBREWS— WITHOUT THE FROTH

Once the toast of Wall Street, U.S. microbrewers—young companies that produce specialty beer at regional breweries—have lost more than two-thirds of their market value since a pack of them went public in late 1995, as earnings have disappointed investors. Pyramid Breweries, which PaineWebber took public at 19 on Dec. 12, 1995, now trades at 3. And Pete's Brewing, taken public at 18 by Morgan Stanley on Nov. 11, 1995, is at 4. For ever lost causes?

Not to investment manager Vince Carino, who sees microbreweries as a prime investment opportunity. The president of Brookhaven Capital has acquired shares in several of these pariahs. His top picks, in which he has taken a 5% stake: Boston Beer (SAM), down to 9 from its initial public offering price of 20 in November, 1995, and RedHook Ale Brewery (HOOK), down to 6 from its IPO price of 17 in August, 1995.

Brookhaven's Choices

STOCK TARGET	MAR. 3 PRICE	52-WEEK HIGH	12-MONTH
REDHOOK ALE	\$6	\$11	\$12
BOSTON BEER	9	11	18

DATA: BROOKHAVEN CAPITAL, BLOOMBERG FINANCIAL MARKETS

"We look for industries or groups in distress that we think are near a recovery phase," says Carino. He thinks both Boston Beer and RedHook, trading at a huge discount to their book values, are likely to double in price in a year.

Carino expects Boston Beer, which makes such brands as Samuel Adams, Oregon Original, and Long Shot at facilities in five states, "will be the first to rebound—in an industry that's now in transition." With microbreweries on the verge of stabilizing, and with capacity and demand about to come into balance, "Boston Beer—which has the best brand names—will be able to turn around faster," argues Carino. He figures that the company will earn \$1 a share next year, vs. an estimated 41¢ in 1998. It earned 37¢ in 1997.

Carino is betting that Anheuser-Busch, which owns 25% of RedHook, will move to acquire the rest of this

producer of nine styles of beer. Carino speculates that Anheuser could make a bid of 11 to 12 for the shares it doesn't already own.

RedHook, which posted a loss of 18¢ a share for 1997 on sales of \$38 million, is expected to be in the red again this year. But Carino thinks it will turn a profit next year. RedHook CEO Paul Shipman notes a standstill pact limiting Anheuser's stake at 25% will run out in October of next year. "But if Anheuser comes to the board to suggest a change, we will consider it," he adds.

THIS RAILROAD IS SET TO COUPLE UP

One huge winner in 1997 was Kansas City Southern Industries (KSU), a diversified rail holding company whose shares more than doubled—from 16 to 35. This year, KSU has continued its upward drive, partly as a result of its long-awaited announcement that it will separate its railroad and asset-management businesses. Many stockholders have taken their profits and bailed out. But not Joe Cornell, president of High Yield Analytics, a Chicago investment firm, who argues that the stock remains way undervalued and is worth north of 50.

This year, the company plans to spin off its Janus Capital and Berger Associates unit, which manages \$75 billion in mutual funds. The unit is worth 36 a share in KSU stock, he figures. DST Systems, a publicly traded information processor serving financial-service companies, is 40.6% owned, and Cornell values it at 10 a share. That leaves KSU's rail operations, which he estimates is worth at least 15 a share.

Cornell expects that after getting rid of its other assets, KSU as a railroad company will find it easier to merge with a transportation company. In a merger, he figures KSU will be worth more than 15, given the stake it owns in a Mexican joint venture which owns an 80% stake in Mexico's largest

rail company, Ferrocarril del Noreste.

"Investors are currently paying very little for KSU's rail operations," says Cornell, "which will be one of the very few remaining railroads that aren't a part of a larger company." He notes that KSU's capacity to move freight from Chicago to Mexico City "could prove very attractive to a larger railroad."

PUTTING RENTRAK ON FAST-FORWARD

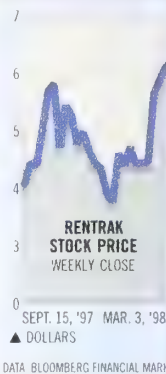
What's stirring up Rentrak (RENT), whose shares rose from 3½ in mid-December to 6½ on Mar. 3? The company, which leases movie videocassettes to some 6,600 rental-retail stores in North America, is expected to double that number soon. How?

Whispers were that major video distributor Blockbuster Entertainment, a Viacom unit, will sign a pact to use Rentrak's proprietary Pay Per Transaction (PPT) system, which allows video stores and other retailers to lease videos instead of buying them. At press time on Mar. 4, Blockbuster and Rentrak announced the deal. This agreement, by almost doubling the number of outlets using the PPT system, will boost Rentrak's revenues and earnings, says one money manager.

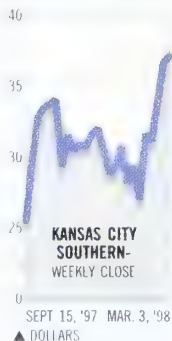
Blockbuster, has 6,000 video stores in North America. Rentrak issued warrants for Blockbuster to buy up to 1 million Rentrak shares at 7 a share. Under the PPT system, Rentrak leases videos to rental stores for one year at about \$8 per tape, vs. a purchase price of at least \$60. The PPT system enables the stores to carry a higher inventory of films at lower cost. The proceeds from the rentals are divided among the store, the film studios, and Rentrak. Rentrak has distribution agreements with 40% of movie studios including Walt Disney and Fox Group.

Exclusive of the Blockbuster pact, Tim Stobaugh of Stonegate Securities expects Rentrak to earn 59¢ a share in the year ended March, 1999, up from an estimated 36¢ in fiscal 1998.

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A LITTLE PRIVACY, PLEASE

Netizens want immediate action from industry and government as consumer-data gathering exceeds the comfort zone



This month, investigators from the Federal Trade Commission will be revving up their Web browsers in a random check of 1,200 sites. Their mission: to see if site operators are posting privacy notices that explain how personal information—such as E-mail addresses, shopping habits, and consumer financial data—is being used and whether it's protected from prying eyes. If the FTC doesn't find a boatload of these policies, the government is threatening to step in and take action.

Normally, such threats would raise hackles in the free-spirited realm of the Net. But maybe not this time. In a new BUSINESS WEEK/Harris poll, a majority of the 999 respondents fingered privacy as the main reason they're staying off the Net—above cost, ease of use, and the morass of unwanted marketing messages. Hardcore Netizens are just a

wary: 78% say they would use the Web more if privacy were guaranteed. Perhaps even more striking, 50% of the computer users polled say the government should pass laws “now” on whether personal data can be collected and used on the Internet.

Such jitters could have a profound impact on the hyper growth of the Internet. Fears that snoops can peek into your private life and track your every movement on the Net could slow the number of people flocking to the info highway, curbing electronic commerce and advertising revenue. Some 57% of poll respondents who use the Net, for example, say Web site policies that guarantee the security of their personal data affect the decision to make online purchases. “It’s clearly a signal to business that they have to be more aggressive in forming privacy controls,” says Alan F. Westin of Columbia University, who helped conduct the poll and who publishes the *Privacy and American Business* newsletter.

So far, the industry’s track record has been found lacking. Many of the most popular spots on the Net still don’t post policies: A BUSINESS WEEK

of the top 100 Web sites found 43% displayed privacy policies. Of notices posted, some were difficult to read and inconsistent in explaining how data are tracked and used. More-TRUSTe, a nonprofit organization that provides a "trustmark" to put on Web sites signifying disclosure of privacy policies and outside auditing practices, has only 75 sites signed up since launching last June—a fraction of its goal of 750. And an FTC sweep in November of 126 children's commercial Web sites found that 86% collected data on children, including E-mail addresses and phone numbers, most without seeking parental consent. Such a lackadaisical approach has angered the government. The FTC made it official after a workshop last June that it would force Web sites to allay consumer

came the whopper last August. Experian, a credit bureau site, pulled the plug on a service that let consumers check their credit history after a nasty chain-letter-like experience in which one person after another was mistakenly given someone else's report.

Patience is running out among some privacy advocates. "For self-regulation to make it, it has to exist—I don't think we're seeing it," says former FTC member Christine A. Varney, an early backer of self-regulation who's having second thoughts. But the Clinton Administration may not have the answer. Administration officials fear regulation won't keep pace with technology, and they say the Web is difficult to police when tens of thousands of new sites pop up every week. "When you have legislation or regulations you can't enforce, it

Pathfinder or Amazon.com. The same sort of data can also be culled from so-called "webstakes," promotional giveaway programs run by companies such as Excite Inc.'s MatchLogic, a subsidiary that posts ads and marketing campaigns for 65 clients across a host of Web sites.

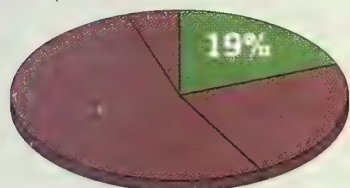
The wave of the future, though, may be companies such as IMGIS Inc. and Intelligent Interactions Corp. These services, which help advertisers and sites post and target ads, are considering or already offer services that combine a smattering of data. That can include registration info, advertiser and Internet service provider data, traffic, and mate-



WANTED ON THE WEB: REGULATION

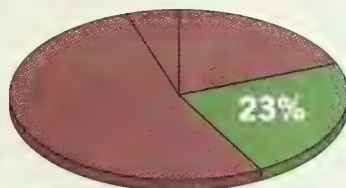
Here are three ways that the government could approach Internet privacy issues. Which one of these three do you think would be best at this stage of Internet development?*

Government should let groups develop voluntary privacy standards but not take any action now unless real problems arise:

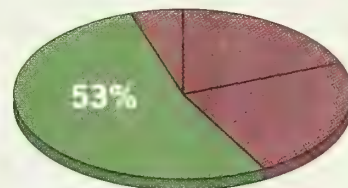


*5% CHOSE NONE OF THE ABOVE OR DON'T KNOW

Government should recommend privacy standards for the Internet but not pass laws at this time:



Government should pass laws now for how personal information can be collected and used on the Internet:



DATA: BUSINESS WEEK / HARRIS POLL

or the government might take on the job. The agency plans to make a tentative report on its findings in June. There also are 32 bills in Congress aimed at Web privacy, ranging from rules to regulate spamming, or unsolicited E-mail, to legislation restricting disclosure of subscriber info by online services. "This is the last year for inaction to demonstrate effective self-regulation," says David Medine, the FTC's associate director for credit practices. That may seem harsh given the site's infancy, but over the past year there have been a number of hair-raising incidents. Just a year ago, the Social Security Administration suspended a service that let people look up personal records, disability information, and benefits estimates, amid public concern that the info could be widely accessed. In January, America Online Inc. provoked an outcry after it proposed giving membership information to partners that could use it to telemarket to AOL's 11 million subscribers. AOL backed down. And then

gives false assurances to people," says Ira C. Magaziner, senior policy adviser to the President.

How do Web sites collect and use the data? Sites amass info with and without consumers' knowledge. The most common way is through "clickstream" data—information about where people go within a site and the ads and content they see. Clickstream data are most commonly collected by so-called cookies, or small data files placed on cybernauts' hard drives when they first visit a site. Whenever a Netizen goes back to that Web site, the site's computer server can read the usage data from the cookies. That info is then stored in a database and can be used to target ads or content, based on the preferences tracked. No. 1 search engine Yahoo! Inc., for example, uses cookies to track how many new visitors come to its site.

Personal information—such as E-mail address, name, street address, age, or sex—is gathered through registration at such sites as Time Warner Inc.'s

rial from direct marketing companies. This is closely watched by privacy advocates. "Is it a big horrible Orwellian plot? No, but marketing people will try to figure out all they can," says Dr. Gary McGraw, senior research scientist at E-commerce security consultant Reliable Software Technologies Corp.

UNIQUE TRAITS. Just so, say Web site operators. Marketers say the ability to gather data and target consumers is what makes the Net unique and is key to attracting advertisers and spurring E-commerce. Many say they are taking steps to keep out peepers. "We definitely believe in protecting our consumers," says Chris Neimeth, vice-president of sales and marketing for the online version of *The New York Times*. "At the same time, though, you can use information to deliver services and ads they would be interested in, rather than seeing something really random." The online *Times*, for instance, has used clickstream info on its 3.2 million subscribers to send E-mail alerting those

who often read the Books section online about improvements to the area.

What will calm the privacy willies? Some say the Web needs clear, consistent site postings about data collection as well as technology that gives users more say-so. Under the threat of regulation, interest in addressing privacy concerns is picking up. Indeed, IMGIS and another company that creates user

profiles, Engage Technologies Inc., joined TRUSTe this month.

Is the Internet being held to a higher standard than direct marketing and telemarketing on terra firma? In a word, yes. After all, consumers who find unsolicited junk mail in their mailboxes every day have let loose personal data that's now being used to sell them everything from soap to sailboats. The

concern is that the Net makes it easier to combine, slice, and dice info from thousands of databases connected to the Web. "People are expecting more," says the FTC's Medine. Now we'll have to see whether they get it from Web site operators or government regulators.

By Heather Green in New York, with Catherine Yang in Washington and Paul C. Judge in Boston

HEADING OFF E-VOYEURS AT THE PASS

When a U.S. Navy investigator concluded that Senior Chief Petty Officer Timothy R. McVeigh was gay based on information obtained from America Online Inc., the incident flared into a controversy over privacy on the Web. But it wasn't technology that failed to protect the sailor. The culprit, according to AOL, was "human error." An AOL customer-service representative confirmed for a Navy investigator, posing as a friend of McVeigh's, that the screen name "Boysrch" was indeed that of McVeigh. The investigator already had obtained a member profile, which had stated marital status as gay.

Protecting privacy, as McVeigh and AOL have learned, is not simply a matter of bits and bytes. In cyberspace, more companies are discovering that safeguarding personal data requires a combination of strict corporate policy and state-of-the-art technology. "The two are inextricably linked," says analyst Kate Delhagen, of Forrester Research Inc.

OPTING OUT. While only a sprinkling of the hundreds of thousands of Web sites have privacy policies today, there's movement afoot. By May, the World Wide Web Consortium, a Net standards body, will come up with a technique that allows people to build a personal profile inside a browser and share it selectively with Web site operators they deem trustworthy. And the Direct Marketing Association has helped 700 companies, including Omaha Steaks, Harry & David, and the Florida Department of Motor Vehi-

cles, draft privacy policies through a service at the association's Web site.

So what are Web operators doing? After the McVeigh incident, AOL tightened its internal policies and training. The online service



FIREFLY'S KLEIN: *He says technology can put the "user in control" of their personal data*

makes names and addresses of members available to direct marketers after screening the mail that will be sent. The company's policy, however, bars disclosure of any other personal data—unless required by a court order. And members can opt out of having their name and address given to marketers. Says AOL CEO Stephen M. Case: "We are extremely sensitive about concerns of privacy and don't want to cross over that line."

New technology is helping them toe that line. At BarnesandNoble.com, for example, visitors can have the online bookstore configured to show new titles in their favorite genres. But with software provided by Firefly Inc. and downloaded from the bookstore site, individuals can choose to turn that feature off. Or, they can set it to alert them when an online merchant is asking for profile information. That way the individual can decide how much data to share. "We won't use personal information to solicit the consumer or sell it as lists," says John Kristie, vice-president of information technology at BarnesandNoble.com. Adds Saul Klein, Firefly's vice-president for strategy: "The whole point is to put the user in control of personal information."

COOKIE DATA. Some Web sites are more interested in where you've been rather than who you are. For example, some areas on Time Warner Inc.'s Pathfinder site require a name and E-mail address and contact registered users with promotional material—but only with their consent. Time Warner also uses cookies, a technology that allows a Web site to track

a person's Web travels. Data from cookies let Time Warner determine what's popular so it can change the mix of programming. "Frankly, we're much more interested in cookie data than in personal information," says Dan Okrent, editor-in-chief of Time Warner Interactive.

In the end, though, to calm the heebie-jeebies, far more Web operators will need to put privacy protection on a par with data collection.

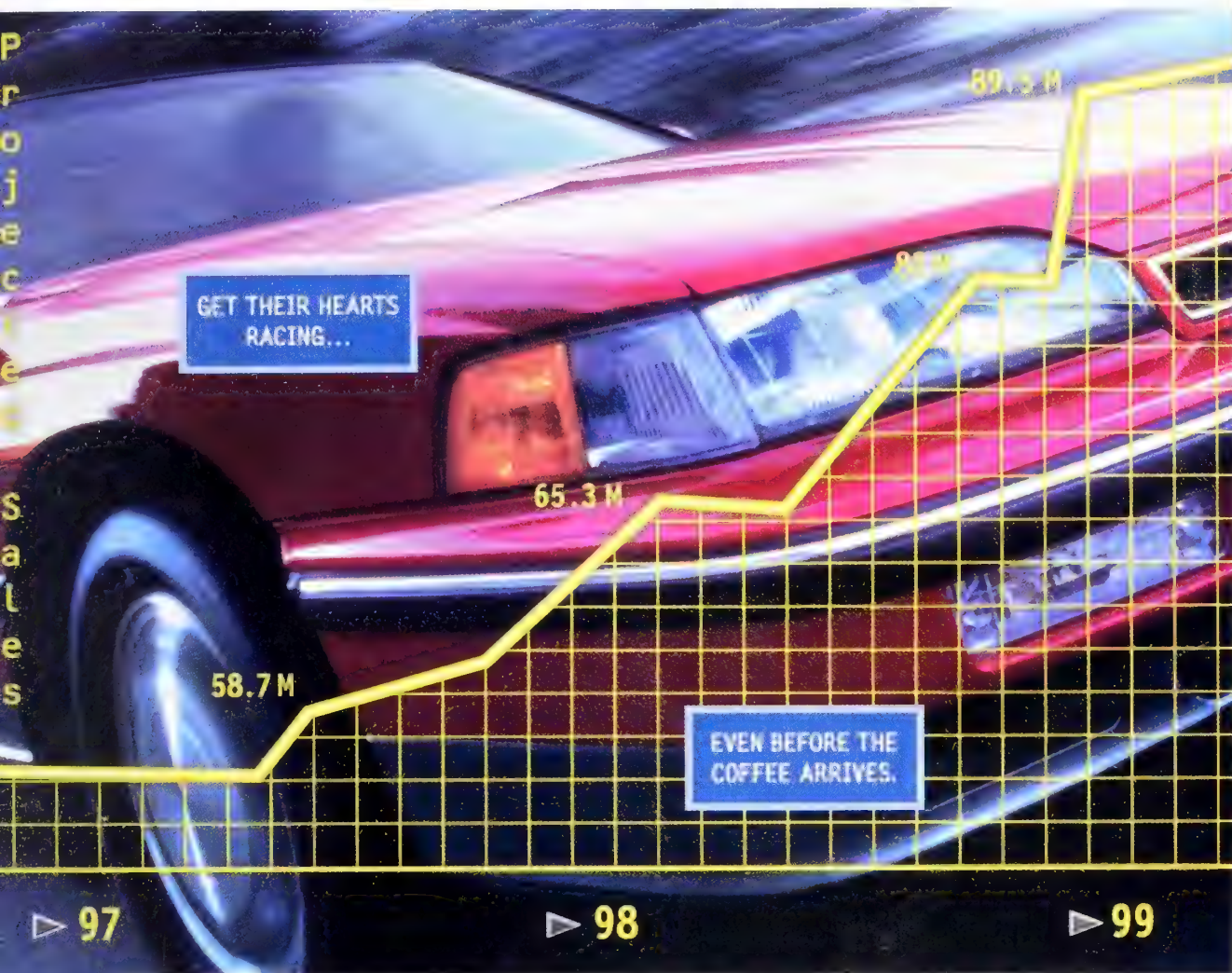
By Paul C. Judge in Boston

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ONLINE INSECURITY

Until now, it seemed nothing could slow the Internet's explosive growth. But sneaky peepers might do it. Worries about protecting personal information on the Net ranked as the top reason people are staying off the



PRIVACY PROBLEMS

Have you personally ever been the victim of what you felt was an improper invasion of privacy, online or elsewhere?

Have been victim	25%
Have not been victim	75%

MAKING THE INTERNET MORE APPEALING

If you don't go online, would you be more likely to start using the Internet, or not, if...

	YES	NO	DON'T KNOW
The cost was reduced	51%	44%	5%
The use became less complicated	53%	43%	4%
You had more control over businesses sending marketing messages that you didn't want	39%	56%	5%
The privacy of your personal information and communications would be protected	61%	36%	2%

WORRY LINES

When you communicate or send a message via the media below, how concerned are you that the content of what you're communicating will be read or overheard by some other person or organization without your knowledge or consent?

	VERY	SOMEWHAT	NOT VERY	NOT AT ALL	DON'T KNOW
By telephone	19%	30%	25%	26%	0%
Using U.S. mail	15%	15%	28%	43%	0%
By fax	19%	29%	26%	23%	3%
By E-mail through the Internet	27%	31%	22%	19%	1%

TRANSACTIONS AND TRIBULATIONS

For each of the following transactions, how concerned are you about the security of your personal financial information?

	VERY	SOMEWHAT	NOT VERY	NOT AT ALL	DON'T KNOW
Paying a restaurant bill by credit card	28%	25%	21%	21%	3%
Giving your credit-card number to a catalog phone service representative	56%	24%	7%	8%	4%
Buying a product online with your credit card	65%	15%	4%	9%	7%
Sending a check as payment through the U.S. mail	21%	24%	28%	27%	0%
Conducting personal banking transactions online	59%	18%	7%	9%	6%

CYBERSHOPPERS...

If you go online, have you ever used the Internet, World Wide Web, or other online service to purchase anything?

Have purchased	22%
Have not purchased	77%

Web—above cost, ease of use, and annoying marketing messages. Even when Web site operators do post privacy policies, people are still wary: 33% don't trust the policies at all; 58% are only a little more at ease.

...THEIR MISGIVINGS...

If you have bought online, when you use the Internet to purchase products and services, how concerned are you about each of these possibilities?

	VERY	SOMEWHAT	NOT VERY	NOT AT ALL	DON'T KNOW
The company you buy from uses personal information you provide to send you unwanted information	31%	34%	31%	4%	0%
The company or one of its employees uses your credit-card information to make purchases without your consent	56%	25%	12%	7%	0%
In the course of the transaction, your credit-card information is made accessible to others who might use it without your consent	56%	28%	11%	3%	1%

...AND WOULD-BE BUYERS' FEARS

If you were to use the Internet to purchase products and services but don't now, how concerned would you be about each of these possibilities?

	VERY	NOT SOMEWHAT	NOT VERY	DON'T AT ALL	KNOW
The company you buy from uses personal information you provide to send you unwanted information	52%	34%	11%	3%	0%
The company or one of its employees uses your credit-card information to make purchases without your consent	80%	12%	6%	2%	0%
In the course of the transaction, your credit-card information is made accessible to others who might use it without your consent	86%	10%	2%	1%	0%

DO PRIVACY POLICIES HELP?

Some companies write and post privacy policies on their Web sites. If you go online, to what extent would a policy that explicitly guarantees the security of your personal information encourage you to...

	A LOT	A LITTLE	NOT AT ALL
Use the Internet more in general	18%	44%	38%
Register on that Web site, providing personal information	12%	44%	44%
Purchase products or service from that company	15%	42%	43%

CAN THEY BE TRUSTED?

If a company posts a privacy policy on its Web site, to what extent do you trust that company to follow the policy?

Trust completely	9%
Don't trust at all	33%
Trust somewhat	58%

EDITED BY KEITH H. HAMMONDS

Survey of 999 adults, including 404 online users, conducted Feb. 18-23, 1998, for BUSINESS WEEK by Louis Harris & Associates Inc. and Alan Westin, publisher of *Privacy & American Business*. Figures may not add up to 100 due to computer rounding. For complete results of this poll, go to: www.businessweek.com or America Online, Keyword: BW

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fig. 1



fig. 2

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ORGANIZERS

PALMY DAYS FOR 3COM?

It has cool new palmtops—but hungry rivals are homing in

The Palm Pilot organizer isn't just a sales success. It's reaching cult status. At the Feb. 18 meeting of President Clinton's high-tech Advisory Committee in Santa Clara, Calif., 15 of the 22 members whipped out the Palm to schedule future meetings. Howard Stern, Robin Williams, and Federal Communications Commission member Michael K. Powell are die-hard

Palmites. All told, more than a million people have snapped up the six-ounce wonder in the past 18 months. And the Palm is not just for keeping track of appointments or phone numbers anymore: There's also software such as AstroPilot to view astrological charts and the Dianameter to keep track of the days since the death of Princess Diana.

Can it get much better than this?

KEEP IT SIMPLE: *Palm's Donna Dubinsky didn't cram in features*

Maybe. On Mar. 9, 3Com Corp. will roll out a version called the Palm III that's more powerful and even slimmer than its predecessor—just half an inch thick at its base, vs. $\frac{3}{10}$ of an inch before. More important, the Palm III will be able to swap data with other Palm wirelessly via infrared beams. That's sure to keep it from hitting the heap like so many other handheld gizmos—from Sony Corp.'s Magic Link in 1996 to Apple Computer's Newton, which died on Feb. 27. "They're a shining star in a graveyard of miserable failures," says J. Gerry Purdy, president of market researcher Mobile Insights. The Palm III will sell for \$400—older models will fall as low as \$200.

LOGO BILLBOARD. But will Palm's star continue to shine? This year, the Palm faces its toughest challenge yet as Microsoft Corp. comes gunning with its latest stripped-down version of Windows for handheld PCs. Starting in April, several palm-size PCs that use Microsoft's new Windows CE 2.0 operating system will hit the shelves from consumer-electronics giants such as Casio Computer Co. and Philips Electronics. The past year CE has come on strong in the past year, and analysts say the latest version—which can support color screens and Web surfing—gives the company its best chance ever. "This is the year the marketing people at 3Com have to earn their pay," says analyst Mike McGuire of market researcher Dataquest Inc.

At stake is not just the future of the Palm but the success of 3Com Chief Executive Eric A. Benhamou's growth strategy. He's banking on the Palm to help boost sales of other products. The \$6 billion company, particularly its growing stable of consumer networking gear, and lift its sagging stock price \$37—down 38% since August.

Benhamou says the popularity of the Palm, which accounts for \$300 million in revenues, will get customers addicted to instant information. That in turn should drive demand for 3Com's bread-and-butter networking equipment, which hooks people into the data highway. The frosting on the cake: Palm helps polish 3Com's brand-name recognition, since most of the company's products are buried inside PCs or in corporate wiring closets. "The logo appears in your face every day," says Benhamou.

A recognized brand is critical to Benhamou's plan. He wants 3Com to dominate the market for consumer network-

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ing products—in contrast to rival Cisco Systems Inc., the market leader in equipment for corporate networks and the Internet. 3Com is already the No.1 supplier of network interface cards, which connect PCs to networks. Last year, it bought the top modem maker, U.S. Robotics Corp. Now, Benhamou wants 3Com to dominate emerging markets for high-speed cable and digital subscriber line (DSL) modems, network chips, and, particularly, home networking—a sector sprouting in the sights of Intel, Bay Networks, and Cisco.

He'll have to protect the Palm from Microsoft first. In just more than a year, products with the older Windows CE have grabbed 23% of the market for handhelds, and now CE is moving into

the palm-size market—where 3Com's device commands a 70% share. Microsoft's advantage is the ubiquity of Windows: Even though Windows CE palmtops can't run desktop PC programs, Microsoft argues that people will be

drawn to the devices because the software looks and feels like the PC version.

And, like the Palm, they can swap data with PCs. "We're giving people a familiar environment," argues Roger Guirajani, Microsoft's group manager for consumer-appliances marketing.

Even more important than Windows' popularity is Microsoft's clout. The software giant has spent as much as \$250 million developing Windows CE, and it's

been able to recruit dozens of developers to write new programs. Even if the latest version doesn't fly, Microsoft isn't likely to give up: It has introduced six pint-size versions of Windows in the past eight years.

PC'S LITTLE HELPER. But this is one market where Microsoft may wind up the underdog. Despite deep pockets and marketing punch, Windows CE has a handicap: It is so stuffed with features that it takes more steps to handle some key tasks than the 3Com device. That's one reason most experts are betting the Palm will continue to dominate the small-device market for years to come. "Microsoft can't duplicate [the Palm]," says Gartner Group analyst Ken Dulaney. "If anything, the gap between 3Com and Microsoft is widening." Dulaney thinks Microsoft won't snatch more than 15% of the palm-size device market.

The Palm's formula for success? It was designed for just a few functions so that it's a companion to PCs—not a replacement. That meant giving it the ability to swap new phone numbers or update schedules with a desktop computer at the touch of a button. "Our mantra was simplicity," says Donna Dubinsky, the general manager of 3Com's Palm division. That has earned it a loyal following. "There's nothing cooler than pulling it out in a meeting," says Barbara Mollenex, an architect with Oldham + Partners in Washington, who uses her Palm for meetings and to track her kids' piano and ballet lessons.

Several strategic alliances will help the Palm expand beyond the digital avant-garde. IBM, which has been hawk- ing the device to corporate customers for the past five months, is about to land some big contracts, including an order for 10,000 units from New York Life, say insiders. Holtville (N.Y.)-based Symbol Technologies Inc., the

leading supplier of handhelds into industry segments, will sell the Palm in June for tracking cargo and meter reading. And wireless-phone maker Qualcomm Inc. will use Palm technology in a new line of portable phones expected late this year—Palm's first foray into the promising wireless phone market.

Look for more firepower ahead. Execs are mum on details, but Janice Roberts, senior marketing vice-president, hints that by this summer customers will be able to access the Net wirelessly from a Palm computer.

And this month, 3Com will back up the Palm with a marketing campaign to build 3Com's visibility with consumers. The multimillion-dollar program will use TV and print ads, Web sites, packaging design, and sales promotions to hammer home the theme "3Com: More Connected." Says Roberts: "We intend to make 3Com a household name."

Benhamou has worked hard at that. In 1995, 3Com bought the right to rename San Francisco's Candlestick Park 3Com Park—a move that brought calls from locals but gave 3Com loads of publicity. "It's hard for pure networking companies to build any kind of brand," explains Benhamou. To do it, he'll have to protect the Palm, his Trojan horse into the home, from a much better known brand name called Windows.

By Andy Reinhardt
Santa Clara, Cal

3Com Brings the Net Into Your Living Room

PRODUCTS	PLANS	REVENUES	1998 GROWTH
MODEMS	Already No. 1 by far, 3Com led the push to 56-kilobit speeds. Now, it wants a leading position in DSL, cable, and wireless modems.	\$1.9 billion	17%
PC NETWORK INTERFACES	3Com dominates the market for cards that plug into PCs and connect them to a network. But cards are being replaced by chips from Intel and others that build networking directly into PCs.	\$1.3 billion	10%
PALM COMPUTER	Today, it's a personal organizer. But by the end of 1998, it could become a pocket-size portal to the Internet through wireless links. Competition will intensify as more handhelds with Microsoft's Windows CE hit the market.	\$300 million	100%
HOME NETWORKING	Network gear for connecting PCs inside homes is the wave of the future. But 3Com faces competition from Intel, Bay Networks, and Cisco Systems.	\$175 million	100%

DATA: BEAR, STEARNS & CO.; BUSINESS WEEK



T FOOD

DUNKIN' DONUTS S ON A COFFEE RUSH

chain offers a dose of Starbucks style, and sales soar

offee buff Melissa LaBarre of Easthampton, Mass., appreciates a good cup of Starbucks brew. But recently, she says, the thrill began thin. "Starbucks is kind of snob-she says. "I don't need the attitude when I'm paying more for a cup." At simple cost-benefit analysis has her to the latest hot choice among ne lovers: Dunkin' Donuts. There, from the dated stereotype of hours-brew, she finds the latest in coffee liness. She chooses from among or more blends of fresh-brewed e, even hot and cold specialty s—all at a fraction of the Starbucks price. Value, together with no-ense service, she says, has made in' her No. 1 coffee spot. LaBarre has tapped a breakfast l. Dunkin' Donuts Inc. may seem antithesis of '90s hip. But the n-largest doughnut chain is giving sophisticated rivals such as Starbucks Corp. and larger competition such McDonald's Corp. a serious battle for

the breakfast buck. Over the past 18 months, the Randolph (Mass.)-based chain has adopted the latest in fast-food cool, from specialty coffee to oven-baked bagels and fat-free muffins. In redone stores, the tacky old pink decor is giving way to a more upscale "ripe raisin" hue. And not content to stop at morning munchies, CEO Robert M. Rosenberg has now set his sights on the lunch crowd. "We have very lofty aspirations," he says.

To the surprise of rivals, many customers are cheering the moves. In the past five months, Dunkin's same-store sales have been up 11.5%, following a 10% jump for the year ended last August. That easily beats the fast-food industry's 2% average. "They've done a terrific job in a very competitive business," says Ronald N. Paul, president of indus-

NEW MENU

Breakfast is just the start. Dunkin' plans to charge into the lunch market by joining some stores with Togo's Eateries

try watcher Technomic Inc. Even normally tight-lipped McDonald's USA has noticed. Concedes CEO Jack M. Greenberg: "Dunkin' Donuts is doing well at breakfast."

And it's doing well with more than just doughnuts. This year, the company, owned since 1990 by British-based Allied Domecq PLC, predicts \$200 million in bagel sales, six times what it sold in the year ended August, 1996. Dunkin's bagel biz is gaining on troubled industry leader Einstein/Noah Bagel Corp., which had total sales of \$303 million last year. That's because the doughnut king has won over bagel lovers like Mark S. Thurber, a Boston attorney who sometimes buys Dunkin' bagels for the office. "I've been very surprised at the quality," he says. "They're as good as anyone's."

NO MORE FRED. Consumers weren't always as happy. Back in 1994, Dunkin's growth, steady for decades, had slowed to a crawl. After 30 years with virtually the same menu and the same tagline—"America's Number One Donut Chain"—Dunkin' badly needed an update. Rosenberg brought in William A. Kussell from Reebok to spice up Dunkin's menu, and its reputation. Kussell nixed the old motto and began a play to become the breakfast king.

That meant longtime pitchman Fred the Baker and his mantra "Time to make the donuts" had to go. Dunkin' retired Fred, replacing him with a \$50 million campaign stressing how much things have changed. The tagline: "Dunkin' Donuts: Something Fresh is Always Brewin' Here."

In addition to bagels, new attention

A RECIPE FOR CHANGE

JUICED-UP JAVA With flavored coffees, iced coffee treats, and a new dark-roast brew, Dunkin' aims to snatch customers from Starbucks and other specialty coffee sellers.

SPRUCED-UP STORES Dated pink and orange decor is out; "ripe raisin" is in. Attractive glass showcases of bagels, muffins, and other new baked goods have increased traffic.

GOOSE-UP MENU To draw a lunch crowd, Dunkin' plans new "combo" stores paired with Togo's sandwich shops or Baskin-Robbins Ice Cream stores.

DATA: ALLIED DOMEQ

went to jazzing up the java. Last summer, Dunkin' introduced Coffee Coolatta, a frozen drink similar to Starbucks' popular Frappuccino. It sold \$75 million worth in four months. And though Dunkin' once made do with regular and decaf, it now proffers coffee flavors from French vanilla to chocolate raspberry and beans by the pound. Overall coffee sales have jumped 40% since 1995.

Rival brewmaker Starbucks won't talk about competitors. But Schroder & Co. analyst Wayne E. Daniels dismisses the comparison. "Dunkin' Donuts may pour a lot of coffee, but what does that matter? It's about class, not mass, at Starbucks," he says. Dunkin' execs say the numbers tell the tale. Starbucks' sales growth at stores open at least one year is about half of what Dunkin' is posting this year. The key, says Rosenberg, has been Dunkin's ability to hold prices down and keep its traditional value-driven customers, while at the same time adding snazzy new products to attract the upscale coffee crowd.

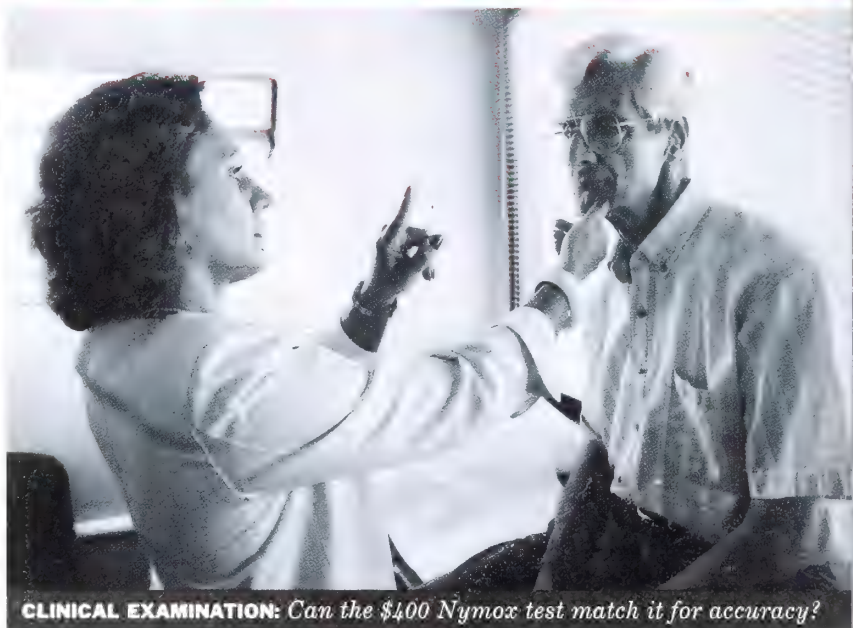
DOUGHNUT DERBY. Ironically, even as Dunkin' broadens its menu, the chain is also benefiting from a resurgence in the popularity of its core product: the lowly doughnut. Overall, doughnut sales rose 10% last year, according to Technomic. Southern sensation Krispy Kreme plans to expand to more than 300 outlets, up from 133 now. Meanwhile, Wendy's International Inc. is gradually rolling out Tim Horton's, a Canadian doughnut chain it bought for \$450 million in 1995 to a handful of northern U.S. cities. But Dunkin', more than 10 times the size of its nearest rival, clearly controls the category. Indeed, it plans to add 300 new stores to its 3,700 this year alone.

For some of those stores, breakfast is just the start. Rosenberg is now planning to charge into the rest of the day with stores that combine Dunkin' with ice-cream giant Baskin-Robbins or Togo's Eateries, a trendy Campbell (Calif.)-based sandwich chain, also owned by Allied Domecq. Rosenberg, who oversees them all, thinks these combo stores can kick growth up to 20% a year, from 15% today. That would double his empire to \$5 billion within five years.

Still, Rosenberg admits his plan to open thousands of combo stores over the next decade is risky. "A lot of [chains] have tried this before, and it has failed," he says. To win at this game, industry watchers say, Dunkin' will have to convince consumers that Togo's—now a relatively unknown 200-store chain—gives them something they can't get elsewhere. But having upped the ante in breakfast, Rosenberg is now hoping to eat the competition's lunch.

By William C. Symonds, reports
Randolph, Mass., with bureau reports

Science & Technology



CLINICAL EXAMINATION: Can the \$400 Nymox test match it for accuracy?

THERAPIES

NO SHORTAGE OF MOXIE AT NYMox

Did the drugmaker jump the gun in selling its Alzheimer's test?

In late 1996, Nymox Pharmaceutical Corp., a little-known Montreal drug company, ran an ad in *TV Guide* for a new diagnostic test for Alzheimer's disease. "Alzheimer's—Now you can rule it out," the copy said. It offered the promise of relief to worried patients and their families. The only problem, some scientists say, was that the ad was misleading. The test was unproven, they say, and the company's claim that it could "rule out" the dread ailment was unsupported by published data or scientific consensus.

The Nymox test detects elevated levels of neuronal thread protein (NTP), a substance linked to Alzheimer's. It is the latest in a long series of attempts to develop a simple test to identify Alzheimer's and conclusively distinguish it from other forms of dementia or neurological disease. But the value of the Nymox test, which costs \$400, is still not clearly proven. And it comes up with a false-positive reading 11% of the

time. The controversy about the way it has been publicized, however, has overwhelmed the scientific debate.

Dr. Norman R. Relkin, an Alzheimer's specialist who directs a memory-disorders program at New York Hospital-Cornell Medical Center, says hawking the test to the public is "reprehensible." The Alzheimer's Assn. derides Nymox' "highly objectionable" sales effort and advises against use of the test, which, because it is not a product, needs no government approvals.

UNDETERRED. Nymox, however, is determined to triumph over its critics. It is going mainstream both in its marketing and its science. It helped fund a study of the test at Massachusetts General Hospital that it says proves its

worth. Armed with the study, the company is shifting to a more subtle marketing tactic: the scientific meeting. On March 16, it plans to host the Manhattan Alzheimer's Disease Conference, bringing several hundred de-

A specialist calls it "reprehensible" to hawk the test directly to patients

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tors, caregivers, and others together with leading Alzheimer's researchers from Britain, Canada, and the U.S.

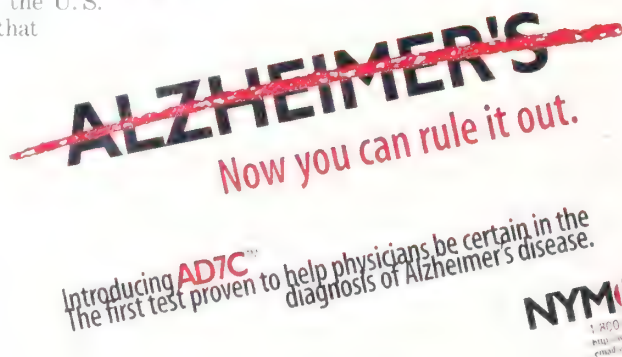
Reaction to the test at that

meeting will be a bellwether for Nymox' own fortunes. The company was founded in 1985 by CEO Dr. Paul Averbach, a neuropathologist who owns about 70% of the stock. Although it has several products in development, the NTP test is the only one on the market. Nymox went public in 1995 by taking over a shell company whose stock traded in Montreal, then watched its Montsoar on the Montreal Exchange from \$2.45 (U.S.) to a high of \$13.50 in mid-1996 on company publicity about the then-unpublished Mass General study. As attacks mounted, the stock drifted down—Nymox was launched on NASDAQ last November at \$6.31 and now hovers at about \$6.

The Nymox story is more than a medical catfight. It shows how commercialism and science can come into nasty conflict. According to U.S. studies, half of all people who reach 90 will develop Alzheimer's, for which there is no known cure. A reliable test could someday be worth hundreds of millions of dollars. Doctors could use it to differentiate between patients suffering from Alzheimer's and those with more readily treatable causes of dementia—such as depression, thyroid problems, or even vitamin deficiency—while drugmakers could use it to assess new therapies.

SKEPTICISM. For 25 years, researchers have sought such a test, only to be disappointed. Another hot prospect, a test for the apolipoprotein E (APOE) gene that is believed to be linked to Alzheimer's, is seriously flawed and can neither predict nor unquestionably confirm the disease, according to the Alzheimer's Assn. Clouding the picture further, in the March issue of *Nature Genetics*, a research team at the University of Pittsburgh reports that people with two copies of a gene called bleomycin hydrolase-g are four times as likely to have Alzheimer's as those with only one copy. The new gene, however, appears to cause Alzheimer's only in people who don't have the APOE gene.

Against such a confusing background, skepticism about the Nymox test is widespread. Nymox acknowledges that the test will yield false positive results in at least 11% of cases. Since no cur-



"It's a pretty valid test," says a neurologist in Atlanta.

"Unfortunately, we do not have enough information on it"

rent test is free of such errors, misdiagnoses could abound, and the chance to treat less dire causes of memory loss or dementia would be lost. Harvard Medical School neurologist Peter Lansbury notes: "A false positive for Alzheimer's is a nightmare."

Plenty of people, moreover, may find the test—now done through a spinal tap and eventually through a urine sample—redundant. When symptoms are apparent, the test's accuracy is little better than that of a neurologist's routine screening. What's more, since there is no cure for Alzheimer's and only modestly helpful treatments, a slight boost in certainty about a diagnosis won't make any practical difference in therapy. Researchers at privately held rival MitoKor Inc. in San Diego say they won't make a test of theirs available publicly until there's a useful drug to go along with it. Says Robert E. Davis, MitoKor's chief science officer: "We see little utility in identifying patients if you can't do something for them." Instead, the company contracts with drugmakers who use its test in their own clinical studies.

However flawed the Nymox test may be, the research that underlies it has promise. Neurobiologist Zaven S. Khachaturian, who heads the Alzheimer's Assn. Ronald & Nancy Reagan Research Institute, says that the Mass General study of NTP, published in December in the *Journal of Clinical Investigation*, is "a very solid piece of science," that could someday spawn a reliable diagnostic test. But this lone study, he and others argue, needs to be replicated, and any test developed out of it needs to be refined.

RESERVATIONS. Besides, say critics, too many questions remain about NTP: For example, what do varying levels of the protein mean in patients, and is it common in many non-Alzheimer's dementias? "The claim that now we can rule out Alzheimer's disease with certainty is simply not substantiated by the data," argues Relkin. Khachaturian questions whether "the marketing effort is warranted by the strength of the scientific evidence." Even clinicians who back the test have reservations. Dr. Eric M. Awad, an Atlanta neurologist, has used the test to help rule out Alzheimer's in three patients—just as Nymox maintained he could. "For lack of better choices at this time, it's a pretty valid test," he maintains. "Unfortunately, we do not have enough information on it."

Averbach, a former emergency-room doctor, blames overcautiousness for some of this resistance. As for his unconventional marketing, he argues that the public has a right to know about new developments, and "some doctors are slower than others" to adopt breakthroughs. Suzanne de la Monte, lead author of the Mass General study, agrees that "people in the neurology and Alzheimer's field are very slow to wake up to something brand new." And, she adds, Nymox' critics "may still be a little miffed" about the ads running before the research had been published.

But reservations persist even after publication of the study. "We need to learn more before I think this is useful," says Peter Davies, a pathology professor at Albert Einstein College of Medicine who is scheduled to speak at Nymox's upcoming New York meeting. In a rush to market, Nymox seems more interested in cashing in on the data than has rather than learning more. A slower course might produce a test that one would say is ahead of its time.

By Joseph Weber in Toronto

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The freedom of Liberty

BY OTIS PORT

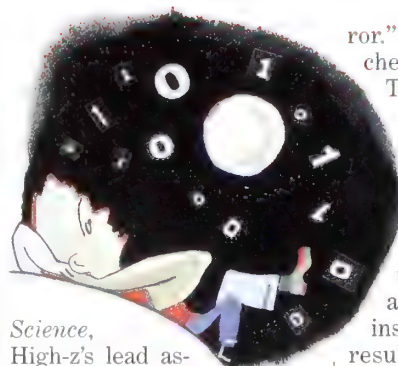
GRAVITY: DEEP MYSTERY TIME

WHILE BLEW IN WITH news about our universe thanks to two international scientific teams. One used the huge Cray supercomputer at Germany's Max Planck Institute in Garching, perhaps the largest supercomputer ever—simulating the evolution of the entire visible universe. The teams peered at exploding stars or supernovas, and space permeated by

a "new" force: antigravity.

Einstein's relativity equations allow for antigravity, but physicists regard it as just a mathematical curiosity, not reality. However, the High-z Supernova Search Team says antigravity seems the only explanation for an apparent speedup in the expansion of the universe since the Big Bang 15 billion years ago. Analyzing its supernova data, the team found the rate at which galaxies are receding from each other is accelerating. So they must be getting pushed apart by antigravity.

In the Feb. 27 issue of



Science, High-z's lead astronomer, Brian Schmidt of the Mount Stromlo & Siding Spring Observatories in Australia, says his reaction was "somewhere between amazement and hor-

ror." So the team triple-checked its data. Result: The group is more than 98% sure that antigravity is the culprit.

Now, Max Planck is gearing up to rerun its simulation "to look specifically at this matter," says Simon White, an astrophysicist at the institute. He expects the results this month. Meanwhile, astronomers around the world are merrily studying the new model, looking for answers to such puzzles as why galaxies formed in clumps and strings. □

FAST, CHEAP, AND CUTTING-EDGE

FINDING A WAY TO PRINT CHIPS FOR THE year 2010 was supposed to cost at least \$1 million. But C. Grant Willson, a chemist at University of Texas at Austin, and a handful of graduate students may have ended it off for roughly \$2 million. They have produced a laboratory circuit with lines so small they border on the ethereal—just 0.08 microns wide. Today's most advanced chips have 0.25-micron lines. Five years ago, with a small grant from the Semiconductor Industry Association, that supports academic research, Willson went looking for a new "film" for printing chips. This so-called resist coating was applied to silicon wafers before circuit patterns are printed with laser light. Back

then, he recalls, engineers believed nothing could both resolve such wispy lines and tolerate the etching that carves circuit lines into silicon. So when optical lithography reached its supposed 0.1-micron limit around 2006, a totally new technology, like X-ray lithography, would be needed.

Now, Willson's crew has handed today's technology a new lease on life. The breakthrough came two years ago, with a chemical concoction that showed promise as a resist. Sematech Inc. coughed up \$2 million to develop it, and engineers from makers of chipmaking equipment, including DuPont Photomasks, ISI, Shipley, and Tropel, flocked to Willson's laboratory to help. One photoresist supplier, Japan Synthetic Rubber Co., has already announced a commercial version of Willson's material. □

TAKE TWO TAXOL AND CALL ME IN THE MORNING

TAXOL IS SOMETHING OF A miracle drug. Derived from Pacific yew tree bark—and since synthesized—it is widely used to treat breast and ovarian cancer. Next, it may solve a problem accompanying angioplasty—restenosis, or the reclogging of blood vessels by scar tissue.

Angioplasty involves inserting a balloon to unclog blood vessels. Some 750,000 procedures are done annually in the U.S., but in 30% to 50% of patients, new clots form. Researchers at the University of British Columbia Hospital and the National Institutes of Health now report that metal supports called stents coated with a slow-release form of taxol prevented restenosis when implanted in the blood vessels of animals.

Dr. Lindsay Machan of British Columbia Hospital notes that taxol-coated stents are also helping check tumor growth in patients with esophageal cancer. "Taxol is like aspirin," he says. "We're finding more uses for it than what it was originally intended for." Catherine Arnst

QUALITY CLAIMS DOWN IN MARKET

IN THE FOURTH YEAR, the award is paying off—and the "Baldrige Index" is performing the Standard & Poor's 500-stock index, now almost 3 to 1. The index shows a composite of companies that have won the Malcolm Baldrige National Quality Award since it exists only

in a computer at the National Institute of Standards & Technology—but it provides a dramatic indication of the value of quality.

NIST calculates the Baldrige Index by investing a hypothetical \$1,000 in each winner, or a prorated amount in the parents of winners that are

divisions without their own stock symbols. NIST also keeps a running account on the stock of Baldrige Award finalists. Although "returns" are not as spectacular as winners', they are nearly double the S&P 500.

Four companies won the Baldrige Quality Award for 1997: 3M Dental Products, Sollectron, Merrill Lynch Credit, and Xerox Business Services. They will share the secrets of their success during a nationwide tour, starting in Philadelphia in May. □

BALDRIGE WINNERS PAY OFF

	1988-1996 INVESTMENTS	VALUE ON 12/1/97	PERCENT CHANGE
ALL RECIPIENTS	\$7,496.54	\$33,185.69	362%
S&P 500	\$7,496.54	\$18,613.28	148%

DATA: NATIONAL INSTITUTE OF STANDARDS & TECHNOLOGY

FOR FURTHER INFORMATION: Go to Business Week Online at America Online or E-mail dtwmar@businessweek.com

EDITED BY AMY DUNKIN

TAPPING HIGH TECH'S LATEST TAKEOFF

If there were ever any question whether technology stocks make good investments, consider what happened in the first two months of 1998. After swooning in December, the top names in technology recovered quickly and drove the NASDAQ to record levels. Some stocks advanced so fast it would take years to make the same return from a certificate of deposit or a T-bill at current interest rates. Dell Computer leaped 61% through Mar. 2, and Microsoft is up 29%. So is it too late to cash in on the latest high-tech boom? Not yet.

Professional technology investors say their worst fears about the financial crisis in Asia affecting high-tech industries have ebbed. And market momentum is clearly in tech's favor. "Investors think that a year from now, all these stocks will be higher, and they're afraid of losing out on the rebound," says Kevin Landis, manager of two high-tech funds at Interactive Investments in San Mateo, Calif. (888 883-3863). Adds Mark Edelstone, principal and technology analyst at Morgan Stanley Dean Witter Discover: "If you look at where the [U.S. economy's] growth is going to come from, it's technology."

HAIR-RAISING RIDE. Despite the recent runup, there are still plenty of bargains around. Some companies are not yet back to their pre-December highs. Seagate Technology, for example, is up 26% this year, to 23%, but it's still below last year's peak of 54. That's a good reminder that high-tech investing can be a hair-raising experience. More than any other sector,

technology can plummet any time for next to no reason. Indeed, Edelstone thinks tech stocks are due for a breather in coming weeks and recommends that investors buy on weakness in the next 30 to 60 days.

Semiconductor stocks are back in favor after being hit particularly hard by the Asian crisis. Edelstone, a chip analyst, likes Intel—despite its recent rise, which has

year record through Jan. 31 of all specialty technology funds tracked by Morningstar, also likes chipmakers. His new fund, Technology Leaders, has Intel as its fourth-largest holding, at 9%. But he thinks there are better bargains among smaller semiconductor makers, including Vitesse Semiconductor, which makes

INVESTING Even value players, who usually shun technology stocks, see opportunities in the sector now

pushed its price-earnings ratio to 22 times estimated 1998 earnings. Edelstone believes Intel's revenues and earnings will grow sharply in the second half as the company sells more high-end microprocessors. At 87%, Intel is trading at a discount to the Standard & Poor's industrials index, whose p-e is 24.

Landis, whose Technology Value fund has the best three-



ships that link copper wire with fiber-optic cable. Vitesse's earnings are expected to rise 37% in the fiscal year ending Sept. 30 as revenues grow over 60%. Despite Vitesse's multiple of 42 times 1998 earnings, Landis thinks the company is "about as bulletproof as you can get in terms of meeting expectations." He's betting that the stock is headed into the 60s from a recent 49%.

Don't care for chipmaker? You may want to follow the strategy favored by James Callinan, a top all-cap fund manager at Peterson Stephens. He's undervalued Internet companies. One of Callinan's picks is Check Point Software Technologies, which makes "firewall" software that is used to provide security on the Net. Check Point is a vital component for Internet commerce, Callinan believes. Its profits are expected to grow 29% in 1998, to \$1.38 a share, and to beat handily 1999

Wall Street estimates of \$1.71, he predicts.

Another Callinan recommendation is Network Solutions, which registers Internet-domain names for \$35 a pop. Some 1 million names were registered last year, but Callinan says the number is expected to grow to 140 million in two years. At a recent 20%, Network Solutions is trading at 41 times expected 1998 profits, well below other Internet companies, such as Yahoo!, which is selling at a mindboggling 197 times estimated '98 earnings. Earnings estimates put Network Solutions' growth at 65% in 1998 and 63% in 1999, making it a relative bargain. Callinan also likes TMP Worldwide. It runs monsterboard.com, a popular Web site for classified ads. At 24, the stock is being valued as if it were an advertising agency instead of an Internet stock, Callinan says. If it were priced like other Net stocks, it would be worth about \$39 a share, he adds.

RARE FANS. Even value players are excited about tech stocks now. Mark Donovan, head of equity research at Boston Partners Asset Management, usually shuns tech companies in favor of steadier, slower growers trading at a discount to the market. But he sees a good value play in EDS, which he thinks is poised to produce strong revenue growth this year after hitting a wall in 1997. At 43%, EDS recently traded at 20 times next year's estimated earnings, well below its usual multiple, Donovan says.

Donovan also likes disk-drive makers Quantum, Western Digital, and Seagate. All these stocks were crushed last fall by concerns about slowing PC sales and excess inventories. Seagate bottomed out at 17% in January, down from last year's high of 54.

But Donovan is convinced the inventory correction has run its course and that

these companies are likely to beat earnings estimates in the next 18 months. Meanwhile, Steven Milunovich, managing director at Merrill Lynch, likes EMC, a powerhouse in the data-storage business. At a recent price of 37%, EMC is richly valued at 28 times his expected 1998 earnings. But Milunovich recommends buying the stock on dips because its rate of earn-

ings, Esther Schreiber, a vice-president at Credit Suisse First Boston, says Microsoft is worth considering despite a high earnings multiple. "Business is going incredibly well," she says.

Schreiber thinks even Microsoft is undervalued based on its expected cash flow and the number of years it should earn an above-average return on invested capi-

Where the Buys Are

COMPANY	PRICE*	P/E RATIO**	
CHECK POINT	40	30	Big in-network security company—and cheap
EDS	43%	20	Good turnaround story
EMC	37%	28	Buy this data-storage company on dips
INTEL	87%	22	Higher-powered Pentiums should boost profits
MICROSOFT	83%	52	NT sales are booming
NETWORK SOLUTIONS	20%	41	Internet name registration at a good value
SEAGATE	23%	NM	Volatile disk-drive maker could see rebound
TMP WORLDWIDE	24	40	Owner of popular job-search Web site
VITESSE	49%	42	Highly regarded chipmaker
WANG LABORATORIES	28%	35	Acquisitions are fueling growth—at last

* Mar. 2

**Estimated 1998 earnings

NM= Not meaningful

DATA: BUSINESS WEEK SURVEY OF JUMPER, FINANCIAL MARKETS

ings growth has accelerated to over 30%.

One way to play the tech sector is to ferret out companies that help manufacturers improve their productivity. Tom Kippola, a Silicon Valley consultant and co-author of *The Gorilla Game*, a new book on high-tech investing, admires i2 Technologies and Manugistics Group, two fast-growing software makers whose programs permit businesses to launch build-to-order strategies. Because the programs let manufacturers save on warehouse construction and inventories, they can break even on their software investments in as little as six months, Kippola figures. If you prefer bigger

tal. Another plus for Microsoft: It's less volatile than, say, Seagate. In the past three years, Microsoft's biggest decline was 19% in a three-week period in December. For a technology stock, that's not bad.

If you don't want to gamble on a high-risk tech stock—which includes virtually every offering—you could stick with a technology mutual fund. Even the best of these gyrate wildly. But if you're eager to own a piece of the latest technology boom, a good mutual fund or a well-diversified group of tech stocks will make sure you don't get left out.

Geoffrey Smith, with Heather Green



HAMMERING OUT A HOUSING PLAY

With low interest rates, fat paychecks, and a fast-approaching new-home buying

season, good times just keep rolling for the nation's homebuilders. Which raises a question: Is there a way for investors to tap residential real estate's persistent strength? Yes, but not the way you might at first think.

You probably want to steer clear of homebuilders. Their stocks are already reflecting the terrific times the industry has enjoyed over the past five years. The group is trading at nearly 21 times 1998 estimated earnings, but expectations of profit growth are running closer to 16%, says Value Line. A gap like that is a warning sign, so a better way to invest in the housing boom may be to buy savings-and-loan stocks. They still trade around 18 times earnings, a discount to expectations of 19% for profit growth. And since October, they've sunk 1.2%, vs. a 22.6% gain for builders.

Behind the poor showing

are worries over how thrifts will profit when mortgage rates are so low. Yet some are better situated to handle that challenge than others. To figure out which are which, we contacted David Ellison, star portfolio manager of

SMART MONEY

FBR's Financial Services and Small Cap Financial funds (888 888-0025). Financial Services, which invests in banks, thrifts, insurers, brokers, and real estate investment trusts, jumped 47.7% last year, while Small Cap Financial, which emphasizes banks, thrifts, and specialty finance companies with market values below \$200 million, soared 58.1%. Ellison is more notable for his 11 years at Fidelity's Select Home Finance Fund. It grew by an average of 21.5% annually on his watch, crushing its peers by more than five percentage points.

Despite last year's gains, Ellison still finds opportunities among thrifts, observing that mortgage lenders have kept bad loans in check. Ellison

favors stocks that are trading at low multiples to expected earnings. A fair range now for small-caps is 14 to 15 times future earnings, and a little more for large-caps. He also screens for book value—1.5 to 2 times for small-caps, a bit more for large-caps. Next, he picks out those with experienced management that rely on a stable base of low-cost deposits to fund loans. And “you don't want institutions that are growing too fast,” he says, because they may be relaxing credit standards or letting costs soar.

Next, we turned to Telescan (www.wallstreetcity.com), which features a powerful search engine and deep database, to screen for thrift stocks with market values of \$1 billion or more that are trading at low multiples to book and to estimates of 1998 earnings. Four names popped out that appear to be solid prospects (table).

Values Among Mortgage Lenders

COMPANY	STOCK PRICE*	P/E RATIO**	PRICE-BOOK RATIO
H.F. AHMANSON	61 $\frac{1}{16}$	15.3	2.5
ASTORIA FINANCIAL	56 $\frac{1}{4}$	16.5	1.8
GOLDEN WEST FINANCIAL	88 $\frac{1}{4}$	13.3	2.0
WASHINGTON FEDERAL	27 $\frac{1}{2}$	13.1	2.0
THRIFT INDUSTRY AVERAGE		18.8	1.6

*Mar. 2 **Estimated 1998 earnings

DATA: TELESKAN, ZACKS, STANDARD & POOR'S, BUSINESS WEEK

GOING UP

Builders aren't the best way to get into this game

H.F. Ahmanson is based in Southern California, but continues to bounce back from its real estate depression of a few years ago. Ahmanson has branched out to Florida and Arizona, among other places. Its fans include noted growth-stock investor Foster Friess, who made the No. 5 holding of \$8.4 billion Brandywine Fund.

TIGHT FOCUS. Next came Astoria Financial. It has stayed closer to its New York origins, most recently via purchase of Greater New York Savings Bank. It's also eyeing Long Island Bancorp. What's more, Astoria, like each of these four thrifts, is stuck to its knitting, with 90% of its loans made on residential real estate.

We also selected Golden West Financial, based in Oakland, Calif. An Ellison favorite, it's run by Marion Horbert Sandler, who owns nearly 19% of the shares. Other big owners include Vanguard/Windsor Fund and Davis New York Venture Fund, whose Christopher Davis calls it “arguably the best-managed S&L in the country.”

Up in Seattle, Washington Federal has expanded throughout the Northwest and has outposts in Utah and Arizona. A slow grower, it enjoys low overhead of only about half the industry average, according to Standard & Poor's (which, like BUSINESS

WEEK, is a unit of The McGraw-Hill Companies), while yielding 3%. Acorn Fund's stock-picker, Ralph Wanger, is among its fans. As with any of these stocks, there's no guarantee Washington Federal will go up. But if you're looking to play the housing industry's boom, thrifts are the place to be. *Robert Bar*

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READY FOR THAT JOB ON THE STREET?

With plans to hire 1,200 new brokers this year,

PaineWebber is desperately looking for more people like Gina Timko. For 15 years, Timko was a registered pharmacist. When she decided to switch careers in her mid-30s, she concluded that being a securities broker was a good way to make more money and use her sales skills. She was right. Today, at age 40, she earns a low six-figure income as a PaineWebber broker in St. Petersburg, Fla.

Not long ago, the securities industry recruited brokers primarily from the ranks of twentysomething college grads. But as Wall Street's bull market continues to fire up demand for financial services, securities houses are seeking out more mature people with varied professional backgrounds to build lasting relationships with clients. A top priority is hiring more women and minorities to better reflect the industry's changing customer base.

CHANGING IMAGE. As full-service firms branch out, the job description of a broker is changing. In fact, most firms have dropped the title "broker" and now use "financial consultant" or "investment executive." Anxious to reverse the image of brokers as obnoxious, overly aggressive stock jockeys, securities houses want their representatives to emphasize full service so clients don't switch to discounters or online brokerages. The new-

CAREERS

generation brokers must fully understand their customers' financial goals and suggest appropriate investments for everything from college savings to retirement. That may mean selling insurance and mortgages in addition to stocks, bonds, and mutual funds.

There's no shortage of applicants for broker jobs. In 1997, Salomon Smith Barney received 70 applications for every one it accepted. If you make the cut, you can expect to earn about \$50,000 in your first year of training and \$70,000 the second. More established brokers make \$120,000 to \$160,000 a year, and top performers can hit \$400,000. But getting to those lofty levels is no picnic. Recruits face a grueling training program of about two years, in which

they're expected to pass three or four licensing exams on the first try. The most critical is the six-hour Series 7 exam, which tests knowledge of investments and industry rules and regulations.

On top of studying and attending seminars, trainees are expected to earn their keep by bringing in commissions. But the really hard work of building a customer base begins after the training period. For the first five years, many brokers work 60-hour weeks and spend six to seven hours a day on the phone making hundreds of cold calls. "The abil-

ity, editor of *Ticker*, a trade publication for brokers. Indeed, 50% to 60% of all recruits drop out within three years.

The going will only get tougher if the stock market ends its long bull run. Previous bear markets have resulted in brokers—especially inexperienced ones—fleeing the industry. When less money flows into the market, it's harder to build a client base and generate commissions.

If you're still interested in making the career switch, your first step is to submit an application at a local branch office. Most firms have Web sites listing information about broker jobs, and some

A top priority is hiring women and minorities to reflect the customer base

ity to accept rejection and ask strangers for money is not an easy task," says Merrill Lynch Vice-Chairman Launny Steffens, who started out as a broker at his firm more than 35 years ago.

New brokers also have to deal with salary swings. Compensation fluctuates depending on monthly commissions and the amount of new assets a broker brings into the firm. "For people who need steady paychecks, being a broker should not be a career choice," warns Jackie

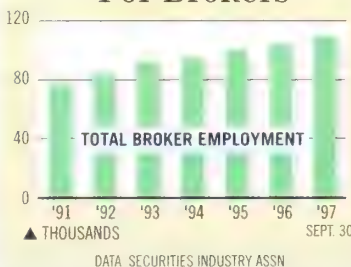
even will allow you to download an application. But the best way to get your foot in the door is to obtain a referral from an employee or even from your broker. Some firms give employees a finder's fee for referrals. PaineWebber pays a \$500 bonus.

During the two- to three-month interviewing process, expect a brokerage house to size up your motivation level and ability to be a self-starter. Don't be surprised if you have to take a personality or intelligence test. Securities firms especially like applicants with a sales background or anything from retailing to real estate.

If you're leery about working in a high-pressure sales environment, another option is to get a job at a discount broker or a mutual fund. You won't make as much as you might at a full service brokerage house. But at least you won't have to twist arms for money. *Adele Malpas*



Boom Time For Brokers





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3M Dental

AHEM: BE KIND TO YOUR VOICE

For Gregg Marano, yelling is part of the job. A foreign-currency trad-

er at M. W. Marshall in New York, he spends his days shouting orders over a cacophony of brokers and customers squawking through speakerphones. Last year, the vocal strain got to be too much. Most afternoons, Marano's throat was so sore he could hardly talk. "You don't realize you're abusing your voice until it starts to go," he says.

Fortunately, Marano, like so many who use their voices for a living, was able to get help. He went to Mt. Sinai Medical Center's Grabscheid Voice Center in New York (www.mssm.edu/ent), one of about a dozen clinics in the U.S. specializing in voice disorders. There, he had surgery to remove what was essentially a callous on his vocal cords. He also learned techniques to prevent strain.

Although voice centers are known for treating performers, many of their patients come from the business world. Typical are trial attorneys, CEOs, and even politicians such as President Clinton, who is prone to hoarseness from allergies and

too much time on the stump.

The widespread use of cellular phones has added to patient rosters. "What used to be quiet time in the car or on the subway is now talk time," says Dr. Robert Osssoff, executive medical director of the Vanderbilt University Hospital Voice Center in Nashville (www.mc.vanderbilt.edu/health/centers/voice.html). The result of all that nonstop gabbing is a raspy voice that often breaks and the constant urge to clear the throat.

THE SCALPEL? While these symptoms can also develop from allergies, infections, or tumors, they are most often due to voice abuse, says Dr. C. Richard Stasney, director of the Texas Voice Center in Houston. During speech, air passing through the larynx,

or voice box, causes your vocal cords to flap together to create sound. Talking too much or incorrectly can inflame the vocal cords (also known as vocal folds). Severe strain can cause bleeding and blister-like nodules that in extreme situations may require corrective surgery. In most cases, though, the problem can be rectified by behavioral and vocal therapies. Costs for an initial evaluation range from \$195 to \$900, and are covered by many health insurance plans.

Your first step back to vocal health, doctors say, is to shut up now and then. Schedule voice recovery time by spacing out speaking engagements and alternating phone calls with paperwork. Also, drink lots of water because it keeps mucous in the throat thin and emollient. "Thin mucous is like hand lotion for the vocal folds," Stasney says.

Avoid dehydrating substances such as caffeine and alcohol. And stay away from antihistamines and decongestants that dry out mucous. Fatty foods and dairy products can provoke an oversupply of mucous, which is equally problematic. Smoking, of course, is anathema.

Another source of irritation is gastrointestinal reflux. This occurs when stomach acid backs up into the esophagus and creates a burning sensation. If the acid washes all the way up to the larynx, it can inflame the vocal folds and interfere with speech. To combat this, doctors advise eating small meals that are not too acidic or spicy. Leaving at least two hours between eating and bedtime can help. And above all, reduce stress, a prime cause of reflux.

Learning to use your voice properly is key to keeping it in good shape. Dr. Peter Woo, clinical director of Mt. Sinai's voice center, says businesspeople are prone to a "Bogart/Bacall syndrome." That's a tendency to reach for a lower pitch, or to shout to sound authoritative. "You don't have to strain your voice to make an impression. But to create a sound without projecting, you need proper breath support. Linda Carroll, a New York speech pathologist, advises swimming and breathing exercises to improve respiratory strength. Posture is also important. "If you slump or your head and neck stick out, it creates a bottleneck for the passage of air," she says. So, to avoid vocal gridlock, straighten up and speak right. *Kate Murphy*

HEALTH

For Healthy Pipes

- Schedule quiet time
- Drink 8 to 10 cups of water per day—more if on a plane
- Eat small meals that aren't too spicy
- Avoid caffeine, alcohol, antihistamines
- Leave two hours from dinner to bedtime
- Don't shout or reach for an out-of-range pitch
- Swim and practice deep breathing to strengthen respiratory muscles
- Maintain good posture
- Stop smoking

WORTH NOTING

■ KEEPING UP-TO-DATE.

Do you need to convert buy, or lease software to your computer recognizes "00" as the year 2000 and not 1900? If you run a business, the Internal Revenue Service will let you deduct most software and consulting expenses incurred beginning in the 1997 tax year for getting PC systems ready for the millennium, says Eileen O'Connor of accounting firm Grant Thornton.



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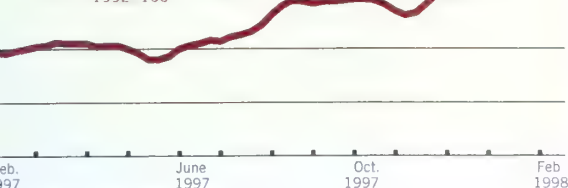
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TECHNOLOGY MARKETING INTELLIGENCE

Business Week Index

PRODUCTION INDEX

Change from last week: -0.1%
Change from last year: 5.5%

PRODUCTION INDEX
Feb 21=131.8
1992=100



The index is a 4-week moving average

Production index declined in the week ended Feb. 21, the fourth consecutive drop. Before calculation of the four-week moving average, the index fell slightly to 132.1, from 132.2 in the previous week. In the latest the index was dragged down by declines in seasonally-adjusted truck and crude-oil refinery runs. Production of steel, autos, electric power, and rail-freight traffic posted gains, while coal output was unchanged.

Production index copyright 1998 by The McGraw-Hill Companies.

TRADING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STOCK PRICES (2/27) S&P 500	1049.34	1034.21	32.7
CORPORATE BOND YIELD, Aaa (2/27)	6.71%	6.71%	-9.1
INDUSTRIAL MATERIALS PRICES (2/27)	95.4	95.4	-12.1
CRUDE OIL SUPPLY, M2 (2/16) billions	\$4,090.1	\$4,082.9r	6.1
UNEMPLOYMENT CLAIMS (2/21) thous.	320	310r	1.3
MORTGAGE APPLICATIONS, PURCHASE (2/27)	217.3	250.8	16.6
MORTGAGE APPLICATIONS, REFINANCE (2/27)	1,526.1	2,005.6	231.1

Sources: Standard & Poor's, Moody's, Journal of Commerce (Index: 1990=100), Federal Reserve, Labor Dept., Mortgage Bankers Assn. (Index: March 16, 1990=100)

INTEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
MORTGAGE RATES (3/3)	5.51%	5.49%	5.16%
COMMERCIAL PAPER (3/3) 3-month	5.45	5.45	5.46
CERTIFICATES OF DEPOSIT (3/4) 3-month	5.59	5.56	5.43
FIXED RATE MORTGAGE (2/27) 30-year	7.22	7.10	7.86
ADJUSTABLE RATE MORTGAGE (2/27) one-year	5.76	5.71	5.73
LIBOR (2/27)	8.50	8.50	8.25

Sources: Federal Reserve, HSH Associates, Bloomberg Financial Markets

data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment, 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

PRODUCTIVITY (REVISION)

Friday, Mar. 10, 10:00 a.m. EST ▶ Fourth-quarter growth in productivity in the non-manufacturing sector is expected to be revised downward to 1.6%, from the originally reported 2.2%. The adjustment reflects the upgrading to the quarter's growth in real gross domestic product, to 3.9% from

motor vehicles, sales are expected to have risen also by 0.4%, following January's 0.5% rise. Weekly survey results have suggested fairly strong buying activity in the month.

IMPORT AND EXPORT PRICES

Thursday, Mar. 12, 10 a.m. EST ▶ Prices of imported goods are expected to have fallen 1% in February, after sharp drops of 1.3% in January and 0.9% in December. Lower oil prices are expected to have pulled down the overall index, but cheaper Asian imports likely resulted in a decline in non-petroleum prices as well. Export prices also declined in both December and January, and likely dipped again in February.

RETAIL SALES

Friday, Mar. 12, 8:30 a.m. EST ▶ Retail sales are expected to have risen 0.4% in February, after edging up 0.1% in January, according to the median forecast of economists surveyed by Standard & Poor's MMS, a unit of The McGraw-Hill Companies. Excluding

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (2/28) thous. of net tons	2,294	2,282#	8.5
AUTOS (2/28) units	113,454	121,685r#	-14.7
TRUCKS (2/28) units	146,115	140,426r#	5.3
ELECTRIC POWER (2/28) millions of kilowatt-hrs	61,327	62,699#	0.2
CRUDE-OIL REFINING (2/28) thous. of bbl./day	13,847	13,805#	3.4
COAL (2/21) thous. of net tons	22,663#	22,423	2.4
LUMBER (2/21) millions of ft.	481.8#	479.9	-3.4
RAIL FREIGHT (2/21) billions of ton-miles	27.4#	27.6	1.9

Sources: American Iron & Steel Institute, Ward's Automotive Reports, Edison Electric Institute, American Petroleum Institute, Energy Dept., WWPPI, SPPA, Association of American Railroads

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (3/4) \$/troy oz.	296.750	292.250	-16.3
STEEL SCRAP (2/24) #1 heavy, \$/ton	140.50	140.50	-3.8
COPPER (2/27) ¢/lb.	77.7	78.0	-33.6
ALUMINUM (2/27) ¢/lb.	68.8	70.3	-13.3
COTTON (2/27) strict low middling 1-1/16 in., ¢/lb.	63.66	62.89	-10.8
OIL (3/3) \$/bbl.	15.12	15.01r	-25.4
CRB FOODSTUFFS (3/3) 1967=100	221.71	220.51	-9.3
CRB RAW INDUSTRIALS (3/3) 1967=100	302.85	299.18	-12.0

Sources: London Wednesday final setting, Chicago market, Metals Week, Memphis market, NYMEX, Commodity Research Bureau

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (3/4)	126.75	128.65	121.43
GERMAN MARK (3/4)	1.82	1.82	1.71
BRITISH POUND (3/4)	1.65	1.64	1.61
FRENCH FRANC (3/4)	6.10	6.09	5.78
ITALIAN LIRA (3/4)	1790.7	1793.5	1703.8
CANADIAN DOLLAR (3/4)	1.42	1.42	1.37
MEXICAN PESO (3/4)	8.581	8.573	8.040
TRADE-WEIGHTED DOLLAR INDEX (3/4)	109.3	109.6	104.8

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars. Trade-weighted dollar via J.P. Morgan.

PRODUCER PRICE INDEX

Friday, Mar. 13, 8:30 a.m. EST ▶ Producer prices for finished goods in February are expected to have declined by 0.2%, following a steep drop of 0.7% in January that was led by the largest drop in energy prices since 1991. Excluding energy and food, the core index is expected to have edged lower by 0.1%. Through January, annual wholesale inflation was -1.3%, while core inflation was zero.

BUSINESS INVENTORIES

Friday, Mar. 13, 8:30 a.m. EST ▶ Manufacturers, wholesalers, and retailers are expected to have increased their inventories by 0.4% in January, after a 0.4% rise in December.

This Week, Online

Business Week presents frequent live conferences and chats on America Online—your opportunity to ask questions about timely topics.

Monday

Larry Samuel, author of *The Future Ain't What It Used to Be*, fills us in on the new cultural trends shaping today's marketplace. It's another event from BW Enterprise, especially for small business and entrepreneurs. **Mar. 9**

8 p.m. EST in the BW Enterprise Chat Room

Thursday

Jump-start your 1997 taxes with the help of tax whiz—and frequent BW Online guest—Jim Vonachen of Clifton Gunderson in Denver. He will answer any and all questions well ahead of the Apr. 15 deadline. **Mar. 12**
9 p.m. EST in BW Online's Conference Room

AOL keyword: BW Talk

Transcripts of all conferences are available for downloading from the BW Online area on AOL soon after each event.



For a free trial diskette including 50 free hours on AOL, call 1-800-641-4848 and mention Business Week.

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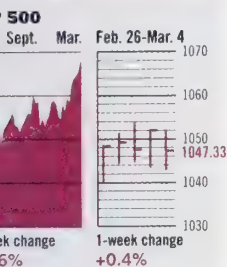
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Investment Figures of the Week

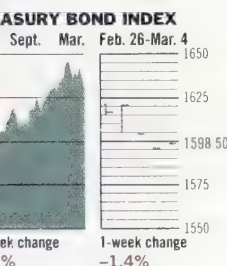
STOCKS



MARKET COMMENTARY

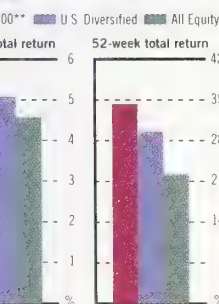
beat week in the U.S. markets. The Dow Jones industrial average broke above 10,500 mark on Feb. 27, climbed to a record high of 10,585 on Mar. 3. Expectations of buoyant consumer spending drove share prices, with retailers, builders, and insurance companies particularly vibrant. But the strong economy sent bond yields falling, with yields rising to 12-week highs. Traders were troubled by some sales figures that showed a stronger-than-expected gain.

INTEREST RATES



Data: Bloomberg Financial Markets

MUTUAL FUNDS



Data: Morningstar, Inc.

U.S. MARKETS	Latest	% change Week	% change Year
Dow Jones Industrials	8539.2	1.0	22.9
NASDAQ Combined Composite	1759.7	-0.4	32.4
S&P MidCap 400	353.9	1.1	33.4
S&P SmallCap 600	193.9	0.6	32.6
S&P SuperComposite 1500	224.9	0.5	30.9

SECTORS	Latest	% change Week	% change Year
Bloomberg Information Age	323.8	-2.2	32.8
S&P Financials	125.5	0.0	33.6
S&P Utilities	233.2	0.4	18.1
PSE Technology	333.1	-1.2	26.8

FOREIGN MARKETS	Latest	% change Week	% change Year
London (FT-SE 100)	5733.1	-0.2	31.5
Frankfurt (DAX)	4709.6	1.6	40.0
Tokyo (NIKKEI 225)	17,095.6	4.5	-6.4
Hong Kong (Hang Seng)	11,350.8	4.3	-15.4
Toronto (TSE 300)	7142.8	2.0	15.1
Mexico City (IPC)	4804.1	1.3	27.7

FUNDAMENTALS	Latest	Week ago	Year ago
S&P 500 Dividend Yield	1.45%	1.48%	1.85%
S&P 500 P/E Ratio (Last 12 mos.)	26.4	25.2	21.0
S&P 500 P/E Ratio (Next 12 mos.)*	20.5	20.1	16.6
First Call Earnings Revision*	-2.49%	-2.77%	-1.69%

TECHNICAL INDICATORS	Latest	Week ago	Reading
S&P 500 200-day average	940.2	934.9	Positive
Stocks above 200-day average	68.0%	65.0%	Neutral
Options: Put/call ratio	0.50	0.54	Negative
Insiders: Vickers Sell/buy ratio	1.61	1.56	Positive

Data: Bloomberg Financial Markets; *First Call Corp.

BEST-PERFORMING GROUPS	Last month %	Last 12 months %
HMOs	22.7	Manufactured Housing 83.3
Manufactured Housing	18.2	Broadcasting 81.6
Apparel Manufacturing	17.5	Specialty Appar. Retailers 79.4
Engineering & Constr.	15.1	Airlines 75.7
Automobiles	14.6	Homebuilding 75.2

WORST-PERFORMING GROUPS	Last month %	Last 12 months %
Transportation Services	-4.2	Metals -38.3
Semiconductors	-2.9	Shoes -35.6
Aluminum	-2.4	Gold Mining -35.5
Pollution Control	-1.6	Engineering & Constr. -22.2
Leisure Time	-0.7	Photography/Imaging -22.1

BLOOMBERG MONEY FLOW ANALYSIS

Rebound ahead? Stocks with most significant buying on price weakness	Price	1-month change
AT&T	62 1/16	-1 15/16
Micron Technology	33 3/8	-4 3/8
Sun Microsystems	45 5/16	-3 1/16
Warner-Lambert	151 7/8	-4 9/16
Teleport Communications Group	55 1/8	-1 7/8
Gateway 2000	40 1/4	-5/8
Decline ahead? Stocks with most significant selling on price strength	Price	1-month change
Microsoft	84 1/2	6 3/32
Dell Computer	131 1/8	23 1/2
WorldCom	38 19/16	2 3/8
Pfizer	87	5 5/8
PeopleSoft	43 3/4	3 15/16
Network Associates	63 3/4	5 5/8

BLOOMBERG MUNI YIELD EQUIVALENTS

Taxable equivalent yields on AAA-rated, tax-exempt municipal bonds, assuming a 31% federal tax rate.

	10-yr. bond Latest week	30-yr. bond Latest week	10-yr. bond Last week	30-yr. bond Last week
GENERAL OBLIGATIONS	4.43%	4.35%	5.02%	4.94%
PERCENT OF TREASURIES	77.05	77.52	83.10	83.48
TAXABLE EQUIVALENT	6.42	6.30	7.28	7.16
INSURED REVENUE BONDS	4.59	4.47	5.24	5.15
PERCENT OF TREASURIES	79.83	79.66	86.74	87.05
TAXABLE EQUIVALENT	6.65	6.48	7.59	7.46

KEY RATES	Latest week %	Week ago %	Year ago %
MONEY MARKET FUNDS	5.13	5.14	4.96
90-DAY TREASURY BILLS	5.14	5.31	5.21
6-MONTH BANK CDS	5.06	5.03	5.00
1-YEAR TREASURY BILLS	5.41	5.43	5.71
10-YEAR TREASURY NOTES	5.72	5.63	6.60
30-YEAR TREASURY BONDS	6.02	5.93	6.85
LONG-TERM AA INDUSTRIALS	6.65	6.54	7.30
LONG-TERM BBB INDUSTRIALS	7.08	6.95	7.64
LONG-TERM AA TELEPHONES	6.95	6.83	7.52

EQUITY FUNDS

Leaders	Four-week total return %	Laggards	Four-week total return %
Montgomery GI. Commun. R	17.1	American Heritage	-10.6
Fidelity Sel. Energy Serv.	14.0	Oppenheimer Real Asset B	-7.3
DFA Pacific Rim Small Co.	13.7	American Heritage Growth	-6.7
Lex. Crosby Sm. Cap Asia	13.1	Comstock Part. Cap. Val. B	-6.0
U.S. Global Inv. China Reg.	13.0	U.S. Global Investors Gold	-5.4
Laggards	52-week total return %	Laggards	52-week total return %
Munder Micro-Cap Equity Y	68.4	Midas	-61.8
Delaware Aggressive Gr. A	66.1	U.S. Global Investors Gold	-61.2
Fidelity Sel. Energy Serv.	63.6	Bull & Bear Gold Investors	-59.2
Fidelity Select Air Trans.	61.8	Invesco Strategic Gold	-58.4
Texas Capital Val. & Grth.	59.9	Gabelli Gold	-51.8

EQUITY FUND CATEGORIES

Leaders	Four-week total return %	Laggards	Four-week total return %
Europe	7.3	Real Estate	-1.1
Unaligned	6.7	Japan	-0.2
Communications	6.5	Precious Metals	0.0
Small-cap Blend	6.2	Diversified Pacific/Asia	1.9
Mid-cap Growth	5.8	International Hybrid	2.1
Laggards	52-week total return %	Laggards	52-week total return %
Financial	40.0	Precious Metals	-43.8
Communications	39.8	Pacific/Asia ex-Japan	-34.2
Unaligned	34.2	Diversified Pacific/Asia	-22.7
Large-cap Growth	33.0	Diversified Emerging Mkts.	-11.6
Small-cap Blend	32.5	Japan	-5.8

are as of market close Wednesday, Mar. 4, 1998, unless otherwise indicated. Industry include S&P 500 companies only. Fundamentals, technical indicators, Bloomberg mon-

ey flow analysis, and mutual fund returns are as of Mar. 3. For a more detailed explanation, write to us or E-mail figures@businessweek.com. NA=Not available **Vanguard Index 500 Fund

PRIVACY: THE KEY TO THE NEW ECONOMY

Call it the economics of privacy. The cost of privacy violation to potential economic growth is rising in America. What was once seen as a threat to civil society is now a clear and present danger to the economic health of the country. Unless privacy is protected soon, the revolutionary potential of the Internet may never be realized. Commerce could be stifled as individuals avoid arenas, virtual and real, where their privacy is threatened. The invasion of privacy may turn out to be the greatest menace to the New Economy.

The chilling effect of the loss of privacy can be seen in Net avoidance. In a new BUSINESS WEEK/Harris poll of adults, 61% not online say they stay off the Net because they feel personal information and communications are not protected (page 102). The same doubts keep 78% of Net users from using it more than they do. Some 80% of people who have never bought anything on the Net say they haven't because of fears that their credit-card data will be given or sold to others. Some 65% of those who do buy things online have the same concern. By a vast majority, people say they do not want to give out financial and personal information to advertisers. They are refusing to register on Web sites.

People don't want the government to have access to their personal data, either. Government proposals to gain possible "backdoor" access to all software through controlling encryption is yet another assault on privacy. In an increasingly digitalized world, every minute fact, every transaction, every communication can be observed and tracked. People know it and feel threatened.

Privacy is being taken away in the name of good intentions. The Net is a new medium, and companies say they need

information on people to target their products, build their business models, and plan their marketing campaigns. The government, in turn, justifies its attack on private communications in the name of combating crime and terrorism. Long goals, indeed. But the long-term cost will be high.

People are increasingly wary of the Net at precisely the time it is approaching critical mass. The advent of below \$1,000 personal computers, WebTV, and other inexpensive options are now opening the Net to its true potential. When the Net was the plaything of academics and the Defense Dept., it had almost no connection to the real economy. Now, it is a major engine for growth, and privacy matters greatly.

Time is running out for the Net community. The public does not trust its promises for self-regulation to ensure privacy. The polls show that people don't believe that the voluntary standards are working. Any spot check of Web sites shows that few make any serious effort to protect privacy. It's no wonder that the public wants the government to step in immediately and pass laws on how personal information can be collected and used. Even Silicon Valley libertarians who believed in voluntary standards for years are longer so sure.

As the economy shifts increasingly from an industrial to an information base, an individual's private data take on an economic utility unknown in the past. So, too, does a person's economic behavior in the electronic realm. Future growth depends on the security of that data and the comfort level with that behavior. Both civil society and economic growth depend increasingly on privacy.

TECHIES ARE SHAKING UP POLITICS. GOOD

Abrash new kind of New Economy politics, different in style and substance from the political games played by traditional Corporate America, is beginning to take form in the U.S. As the economic center of gravity shifts to Silicon Valley and as the clout of information-based companies grows, the nation's political agenda is beginning to change. The Washington Establishment is betting it will tame the kids from the Valley. Let's hope not.

Valley boys (and girls) believe they are creating the future and that anyone who questions them simply doesn't get it. So New Economy politics is infused with attitude, a mixture of irreverence, self-confidence, and elbows-out combativeness. The Valley approach is situational. Instead of primarily relying on permanent political action committees or lobbyists, they tend to form coalitions around specific issues, do battle, and then disband. It's guerrilla warfare.

The issues dear to the Valley cut across conventional liberal and conservative lines. The New Economy agenda calls for

more immigration, but of highly skilled, technologically literate people. Securities reform to block class actions is important, since they threaten initial public offerings and stock options. Intellectual property is a biggie, since this is the capital that Silicon Valley thrives on. Blocking taxation of Internet commerce is a major issue, for obvious reasons. And keeping the government out of encryption is good for exports—and privacy. On antitrust, the New Economy folks split between pro-Microsoft and those crying "monopoly."

The New Economy has grown so fast that it must now interact with the rest of American society. The policy conflicts now appearing are harbingers of things to come. We think the Valley boys could use a bit more polish and just a dash of respect when they go to Washington. America loves a maverick, but not one who's above the law. If the fresh-faced New Economy folks can ride out of the West and freshen Washington out of its entrenched, and money-soaked, ways, the country will be theirs.

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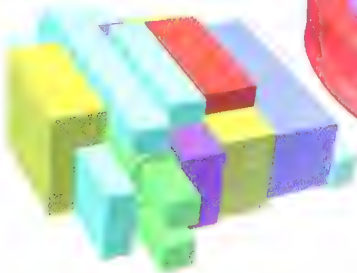


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Intrepid, so where in the world did we find more useable space? Why, in cyberspace of course. Despite the new Intrepid's slipperier shape, our proprietary design and assembly software enabled a slight increase in cabin space and a considerable



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space to give Intrepid a larger glove box.

Of course more space wasn't all we found in cyberspace.

The new Intrepid seats provide enhanced lateral and lumbar support with increased comfort.

The ergonomically correct instrument panel is as sleek as the exterior, with integrated center console and soft-touch surfaces. The horn, of course, is right in the center of the steering wheel, where it belongs. Even our most powerful computers couldn't find a better location than that.



Cyber

BusinessWeek

23, 1998

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THE NOSTALGIA BOOM



BURLINGAME

MAR 13 1998

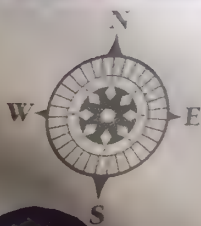
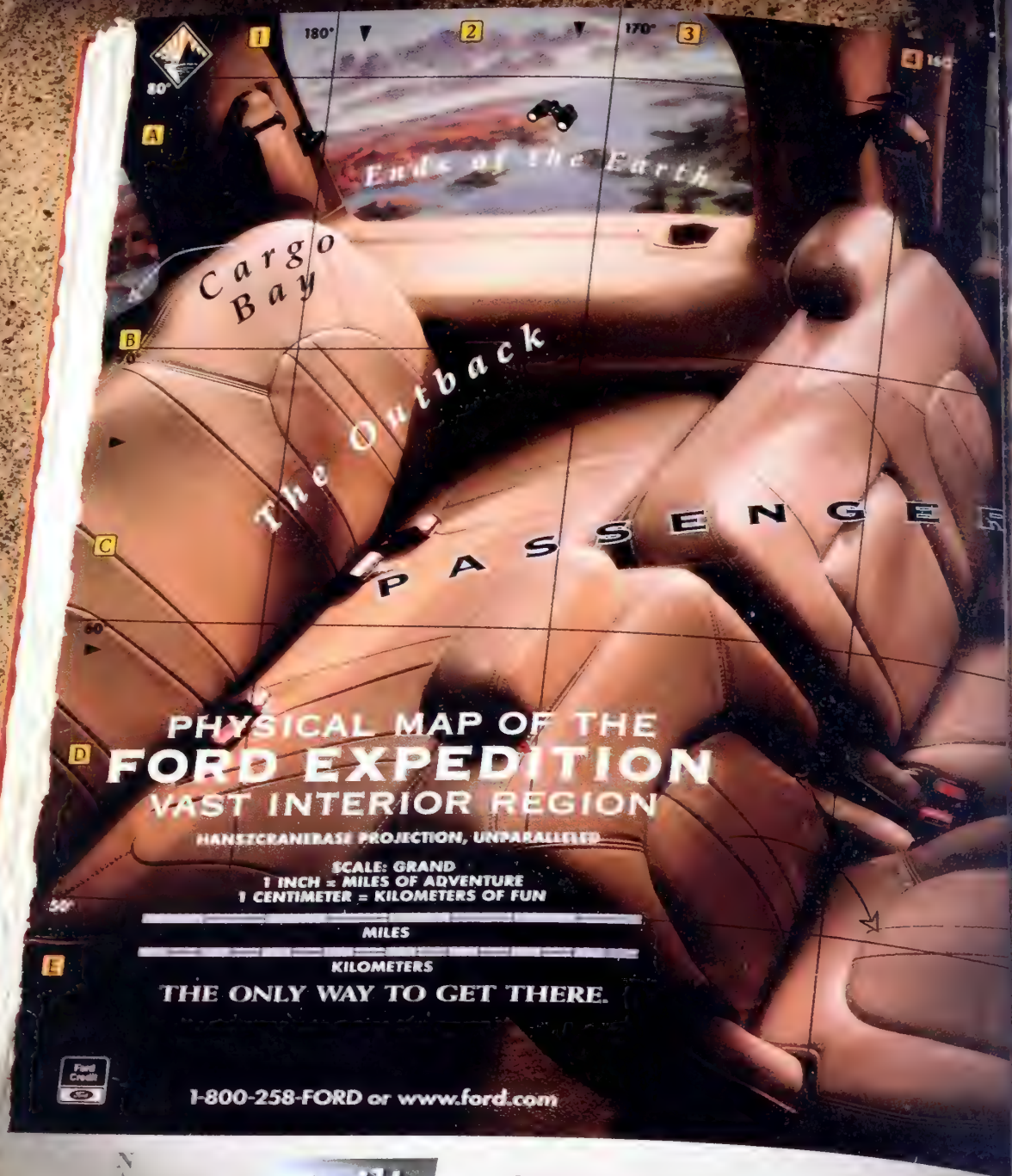
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Americans aren't merely misty-eyed over the past, they're willing to pay big bucks to relive it page 58

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Cover Story

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Old is new again, from Volkswagen Beetles to Burma Shave signs to ballparks in which your grandfather would have felt comfortable. In these anxiety-ridden times, it seems a lot of people yearn for the good old days. And that's what marketers are giving them, offering products or ads that evoke golden days and youth that never fades

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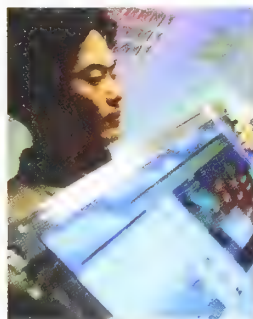
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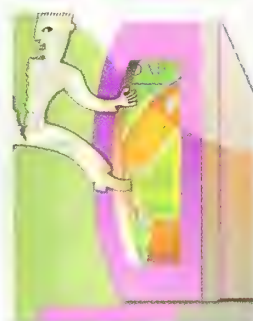
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R LEAGUE SOCCER'S FUTURE

arting a new season that could
most important yet

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a big online newspaper venture,
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Up Front

EDITED BY ROBERT McNATT & LARRY LIGHT

REVOLVING DOOR

IT'S CUSTOMIZED INTELLIGENCE, NOT SPYING

WORRIED ABOUT BUSINESS prospects in Indonesia or Brazil? You're not alone. But three former Clinton Administration insiders will help you figure it out—for a fee.

The three ex-officials have formed Newmarket Co. It offers advisory and customized information services on 22 emerging markets. It also sells data on economic and political trends to institutional investors and big companies.

Anthony Lake, a former national security adviser, is chairman. Also on board: former CIA chief John Deutch as chairman of its advisory board. The third man on the



LAKE: Focusing

team is President David Rothkopf. He promoted emerging markets while working at the Commerce Dept. and predicted last year that some were overheating. His prescience has attracted clients. And although ex-spymaster Deutch is aboard, Rothkopf says he doubts any former spooks will be on the payroll.

Newmarket already has boosters. Michael Conelius, manager of the T. Rowe Price Emerging Markets Bond Fund, says the firm comes along at the right time because of the dearth of reliable data about these markets. *Stan Crook*

TALK SHOW "It's time to show his cards." —Senate Majority Leader Trent Lott (R-Miss.), Mar. 7, on Kenneth Starr's progress

"He can't complete the work as long as he is dealing with stonewalling." —Lott, Mar. 9, after a Republican uproar

WEATHER WATCH

IF IT RAINS, ARE YOU COVERED?

RAIN INSURANCE MAY SEEM A quirky idea in most places. Not in California, where torrential rains have prompted a scramble for rain insurance. For insurers, if not for anyone else, there's a golden lining in El Niño's storm clouds.

For years, rain insurance (not for flooding, mind you) has covered washouts at movie shoots, outdoor concerts, and the like. Premiums were estimated at \$15 million in 1997. Now, the El Niño storms have prompted big players like Cigna and AIG to introduce products that offer businesses weather and damage risk protection. Good Weather, a Salem (Mass.) agency, says it sold 1,000 storm policies for Reliance National and Lloyd's of Lon-



SINGING: Insurers like rain

don last year, 43% more than in '96. Rain damage totaled \$81 million in California in January and February. But insurers are sanguine. "Historically it's been a profitable business," says Sal Nocife, a Reliance exec. As more businesses sign up, claim-paying insurers may even be happier after the state dries out. *Susan Jackson*

REALITY BYTES

KEEP YOUR DIGITS OFF THAT AD!

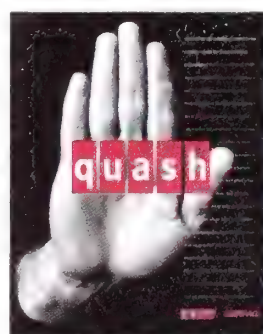
IMITATION MAY BE HIGH flattery, but in the technology business it can also be worth a lawsuit. Digital Equipment took offense

—and HP pulled the ad. Digital and Compaq related with a co-branded ad even though their merger is finalized—in several business

publications. The ad doesn't use HP's name, but features the word "Quash" and seeks to dismiss "rumor" about the future of Digital technologies.

But like the Hatfields and the McCoys, the companies are still at it. HP now

plans mid-March ads offering Digital customers up to 30% off the original purchase price if they trade in their computers for HP's. Techies may be cerebral, but when it comes to their ads, they can be nasty too. *Paul Jude*



HALT! Digital's bit

SLUGFESTS

REACH OUT AND PAY SOMEONE

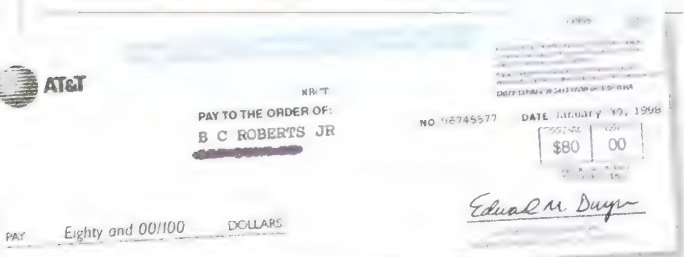
THE TRUCE IN THE PHONE wars has broken down, and there's nowhere to hide. MCI Communications is accusing archrival AT&T of flooding the market with checks to attract new customers, despite its assertions that it's curtailing the practice. The idea behind the checks, which typically run \$50 to \$100, is simple: Cash one, and your long-distance provider is AT&T.

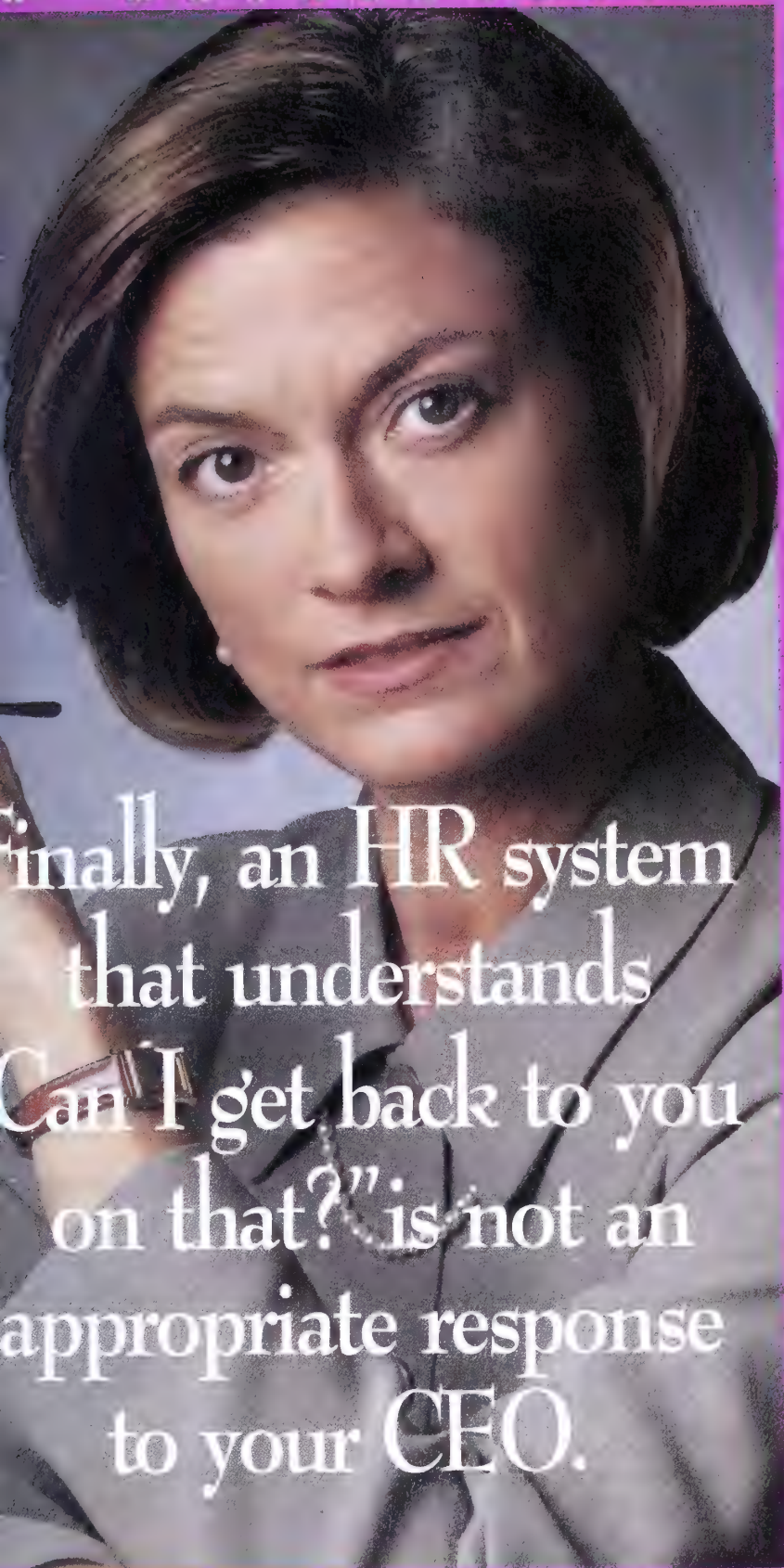
MCI estimates AT&T sent out checks worth \$368 million in January, up from \$70 mil-

lion a month in fourth-quarter '97. "AT&T continues to pay customers to switch carriers, even though it says publicly that the tactic is misguided," says an MCI spokesman.

Both companies agree the number of checks sent out by AT&T in January has fallen since January, 1997. But MCI says the value of those checks rose, because the average check increased by 71%, to \$72. AT&T would not comment on the checks' value.

AT&T even wooed MCI Chairman Bert Roberts with an \$80 check in January, \$8 more than average. It wasn't enough to make him switch. *Peter Elstrom*





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Up Front

VACATION NATION

ROCKING DISNEY'S BOAT



E. T. IS PUTTING THE SQUEEZE on Mickey Mouse when it comes to Florida vacations. Walt Disney has big plans to enter the cruise business. But delays in the delivery of its new cruise ship have moved its maiden voyage back to the end of July. As a result, movie and theme park rival Universal Studios, producers of *E. T.*, is seeing an upswing in those choosing its vacation packages.

Universal's vacations tie a stay at its theme park in Orlando, or three others in the area, with a cruise on the Carnival line. They are similar

to what Disney offers—a cruise and a stay at Disney World. Don Gleason, president of Universal Travel, says business is up because of the ship problems at Disney. "Bookings have been very strong," he says. "We definitely have seen the activity pick up."

Disney, meanwhile, is working to please disgruntled passengers, who can get a full refund or rebook at a discount. Disney now insists that the inaugural July 30 sailing is "300% guaranteed." Still, the three-month delay hurts Disney all the more because the cruise business is booming. Says one travel agent: Bookings everywhere are "definitely up" because customers want the "Titanic experience." Presumably, that means just the romance. *Dennis Blank*

BOOKED: Carnival cruise ship

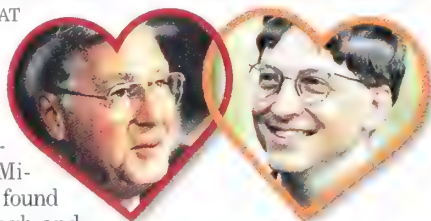
HONCHOS

A FRIEND OF BILL-GATES, THAT IS

THERE'S NOTHING THAT Janet Reno, schoolmarm to Corporate America, would like better than to rap Bill Gates's monopolist knuckles. But Microsoft's bad boy has found a friend in the rough-and-tumble capital schoolyard.

His new bud is none other than House Majority Leader Dick Armey. A former college economics professor with a fondness for cowboy boots and ties bearing Adam Smith's image, Armey is a fierce free-market advocate, and Gates is one of his capitalist heroes.

Armey finally met his highness of high tech in February during a West Coast political swing. He came away from the session with a coveted souvenir: an autographed copy of Bill Gates's book. Ever vigilant about congressional



COMRADES: Armey, Gates

ethics, Armey quickly noted that the present was "permissible under [House] gift rules."

Armey would be a useful friend for Gates to cultivate. As majority leader, he directs the day-to-day legislative calendar of the House of Representatives and is a possible successor to House Speaker Newt Gingrich. On the other hand, Gates has a little juice with the Armey family: Armey's stepson, Scott Oxdine, works in Dallas—for Microsoft. *Richard S. Dunham*

DRAWN & QUARTERED



SPORTS BIZ

ARABIAN HORSES FINISH OUT OF THE MONEY

IT WAS SUPPOSED TO BE THE auction that spurred Arabian horse racing to keep pace with its glamorous Thoroughbred counterpart. Alas, it wasn't to be. On Mar. 7, 27 offspring of Arabian champ Wiking went on the block in Ocala, Fla. But only nine found new owners.



ARABIAN: Auction bust

That was a major disappointment for the industry, which has 1,000 racing horses in the U.S. Purses for Arab racers totaled only \$4.5 million in 1997, horse feed compared with the hundreds of millions pulled in by Thoroughbreds. But as the num-

ber of Thoroughbred races has fallen, Arabian racing has grown as a cheaper alternative for racehorse owners.

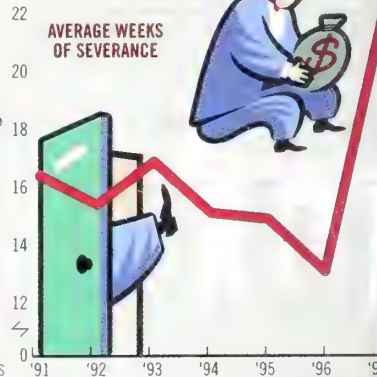
So why did the auction net only a feeble \$201,000? A spokeswoman for Town Country Farm, Wiking's stable, said there were so many good horses, buyers could afford

pick and choose. "Even if a lot didn't sell," she adds, "it's only because the owner thought they could sell them and make more money." But Arabians have a way to go before they land in the winner's circle. *Nathan Estess*

THE BIG PICTURE

SWEETER SEVERANCE

Severance is more generous lately. That's good news for downsize victims, who continue to proliferate as companies cut costs. In prosperous times, employers can afford the extra money.



DATA: CHALLENGER, GRAY & CHRISTMAS

FOOTNOTES Companies that use the Internet to recruit candidates: 1995, 0%; 1996, 26%; 1997, 37%

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on European Monetary Union.
Jonathan Thaler
New York

the Y2K problem is much more serious than even the alarmists are aware. In 1972, the hospital I worked for mistakenly sent out more than 10,000 medical bills threatening immediate legal action if not paid. I was the accounts-receivable supervisor at the time and the error was caused by a computer program that thought the date was 01/01/1900.

Two sitting Supreme Court Justices, a retired Justice, Attorney General Mitchell's maid, Bobby Kennedy's daughter, members of Congress, and various other dignitaries were threatened with civil suits. Patients couldn't use the phones because of the crush of incoming calls. The phone company threatened to sue the hospital and shut down the phone system in one quadrant of the District of Columbia was completely affected.

This mistake will happen 1,000 times around the world in the year 2000 and will probably bring "modern life" to a grinding halt for a few weeks. Consider the sound the alarm, particularly in the editions in other countries.

John Gochenouer
Andreas School of Business
Barry University
Miami Shores, Fla.

MILKEN NO SAINT

Paul Craig Roberts has canonized the great capitalist saint in "Who did more for mankind, Mother Teresa or Mike Milken?" (Economic Viewpoint, Mar. 2). He is in a long line of apologists for the machinations of Michael R. Milken. The idea appears to be that we should forget the blessings bestowed on the economy by Milken through the channel of the junk-bond market.

This makes little sense. Milken merely moved funds from one use to another. To make a lasting positive impact on the economy, his operation would have to raise the level of savings and investment, increase technological advancement, or channel funds from low-productivity to high-productivity uses.

There is no indication that any of this occurred. Careful studies of junk-bond financings during these years do show that the recipient firms had below-average productivity growth. And finally there is nothing in the macro data to indicate that any of the three conditions manifested themselves in the 1980s.

Arnold Pearlman
Sandy Hook, Conn.

Materialistically speaking, I suppose Milken did more for mankind than Mother Teresa, but Roberts must be aware that there is more to life than materialism. It is a dismal view of the world that accounts for no more than money.

It is also unnecessary to imply that anyone who criticizes capitalism is an ideologue who refuses to "give up communism." Capitalism has many fine attributes, but social justice is not high on the list. It is appropriate to observe that and to think about what can be done to

ameliorate capitalism's shortcomings.

Daniel M. Warner
Bellingham, Wash.

The "greed" Paul Craig Roberts would posit as a virtue is to be found in all those who ignore the responsibility that freedom requires. Jesse James, Al Capone, and others exercised economic freedom in their markets. They "earned" the rewards of "merit, ability, luck, and success." They were also felons.

That is no problem for those who

Will Takes



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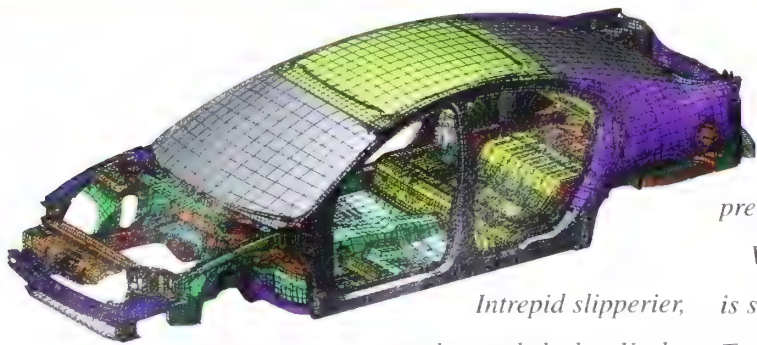
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more accommodating as well, with even more useable space than the previous Intrepid.

What's more, this Intrepid is structurally superior. Torsional stiffness has been increased by a full 37%, yielding a quiet, athletically agile car. And while Intrepid's sleek new lines

are a visual delight for onlookers, its low hood and large windshield are a visual delight for drivers who appreciate a good view of the road.

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Readers Report

equate freedom with greed and make economic capitalism into a moral absolute. [But] such a hypothesis is so foreign to the American value system as to guarantee its ultimate rejection. "Absolute freedom" is not moral; only "responsible freedom" is. I am free as long as I do not exploit my neighbors' rights. That is not communism; it is the foundation of American constitutional government.

James Schulte
New Berlin, Wis.

'INSULT AND BRAVADO' WON'T ALTER AN ANALYST'S FACTS

Here's what's important about "Qwest: One analyst doesn't spoil a good year," (Readers Report, Mar. 9). Please notice that CEO Joseph P. Nacchio did not challenge a single statistic that Gene G. Marcial included in "Pick up this call. Hang up that one" (Inside Wall Street, Feb. 23). He couldn't because the facts were correct. That left him with only insult and bravado.

Analysts can laud a management if their employers are also the company's investment bankers. But there is a vast difference between prepaid "hype" and true analysis. And Nacchio's inflated stock is critical to his ability to do deals like the one announced on Mar. 9 to acquire LCI International Inc.

It's amusing that Qwest Communications International, a self-proclaimed leader of the telecom revolution, has a poor internal phone system. Nacchio is unaware that Marcial called him at least once, and that I called the head of investor relations three times. I'm still waiting for a reply. My satisfaction comes from seeing that IXC Communications has risen more than 40% since your story appeared, while Qwest has stalled out.

Joan E. Lappin
President
Gramercy Capital
Management Corp.
New York

MEDLEY CREDIT TELLS ITS STORY

"Investors beware: Chop stocks are on the rise" (Cover Story, Dec. 15) left misleading impressions about Medley Credit Acceptance Corp. and myself. According to the article, warrants offered by Medley Credit in its recent initial public offering were being used to reward disgruntled customers of a brokerage called PCM Securities Ltd. It said I was directly connected to PCM, and, additionally, that Medley Credit was not

a viable business entity with a working telephone number.

The fact is that I am not an officer of PCM. I had been president of the general partner of PCM but left more than a year and a half ago when the firm was sold to Mitchell Financial Group. I had contemplated doing a public offering for Medley Credit during the time I was involved with PCM and when we sold the brokerage firm. Eventually, we pursued the path of a self-directed underwriting rather than be involved with any micro-cap securities firm.

We do not have any arrangement with PCM Securities now nor have we had a viable agreement in the past for them or any firm to underwrite our initial public offering. As a result of the article, several potential investors pulled out of their agreements with Medley, thus threatening the completion of the IPO. The IPO was recently completed successfully with the sale of more than 1.2 million shares, but it was placed in extreme jeopardy as a result of the misinformation.

Regarding our warrants, I cannot comment accurately on what a PCM broker did or did not do. Our warrants had an exercise price "above" the offering price, and the company has an extraordinary call with respect to the warrants. This was done to encourage holders to exercise the warrants. As for unscrupulous promoters as described in the article—neither I nor any employee of Medley Credit are involved in any way with such business.

As for not being able to reach Medley in a timely manner, all anyone has to do is call Miami information.

During our self-directed offering, I took great pains to distance our company from the micro-cap underwriting world and its inherent problems with the belief we can grow and eventually list on the American Stock Exchange. While small companies have been going public for decades, it is unfortunate that the types of things described in the article continue to muddy the waters.

Robert D. Press
Chairman & President
Medley Credit Acceptance Corp.
Miami

Editor's note: BUSINESS WEEK disagrees with Press's effort to distance Medley Credit Acceptance Corp. from PCM Securities, and in fact BW understated the ties between Medley and PCM. According to the most recent Medley filings with the Securities & Exchange Commission, Press and Steven Edelson control Performance Capital Management, which runs PCM Securities pursuant to

a management contract. According to Medley filings, Edelson is the PCM principal running the firm's day-to-day operations, and a person who answered the phone at PCM in December indicated that Press and Edelson both worked there. Edelson and Press are listed in the most recent Medley filing, dated Dec. 24, 1997, as "control persons of Medley Group Inc.," the company that held virtually all Medley stock before the IPO. And Edelson was chairman of Medley until late July. His departure was not disclosed in Medley filings until after the article appeared.

Lastly, efforts to obtain comment from Medley before the article was published were fruitless because the phone number listed in Medley filings was disconnected, and, as Press has acknowledged to BUSINESS WEEK, no listing for Medley was available from Miami information before the article appeared.

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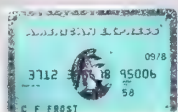
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THE WEALTH AND POVERTY OF NATIONS
Why Some Are So Rich and Some So Poor
 By David S. Landes
 Norton • 650pp • \$30

IS CULTURE THE KEY TO GROWTH?

It is perhaps the most fundamental and important question in the study of economics: What makes nations grow? If economics is to have any relevance at all in our lives, it must provide some answers and give people and governments a few pointers. The great economists of yore—from Adam Smith to Alfred Marshall and John Maynard Keynes—always kept the big picture in mind and attempted to address it in their various writings. In recent times, though, few economists have examined the growth issue head-on, preferring to focus on narrow, often irrelevant topics.

But the wrenching changes wrought by technological advances and globalization have made the growth question fashionable again, and economists are gamely trying to meet the challenge. Theoretical economists are examining the components and nature of growth, while empiricists are totting up results and making national comparisons. A fertile area of research is the past, which provides countless examples of what worked to promote growth and what didn't. Yet a paucity of reliable data often prompts analysts to settle for slippery sociocultural explanations.

David S. Landes, an economic historian at Harvard University, bravely searches for clues to why some societies are economic successes and others economic failures in his new book, *The Wealth and Poverty of Nations: Why Some Are So Rich and Some So Poor*. The book is by turns familiar, fascinating, and irritating. Familiar, because others have described the particulars of, say, Britain's Industrial Revolution equally well. Fascinating, because Landes picks and chooses excellent illustrative details and offers interesting takes on Spain, China, Japan, Egypt, and other countries. And irritating because of Landes' opinionated and crotchety style, which is particu-

larly on display as he drags the reader into academe's culture wars through gratuitous and repeated jousts with other scholars. It's possible to learn a great deal from this book, but the reader will have to shoulder the dross along with the gold.

Landes, the author of numerous widely cited and highly regarded books, has undertaken nothing less than an economic history of the world. Although he ranges widely in his choice of locales, the emeritus professor is admittedly and unabashedly Eurocentric: "As the historical record shows, for the last thousand years, Europe (the West) has been the prime mover of development and modernity."

Landes credits the West's economic success to a few key variables: the ability to use, adapt, and invent new technologies; the encouragement of literacy and learning; the relative openness and flexibility of political systems and social institutions. Innovations that spurred growth in the West included the essential—eyeglasses, whose widespread adoption in 15th century Florence and Venice had a phenomenal effect on productivity—and the serendipitous—the discovery of dyes, which led to the development of the German chemical industry.

Landes' concern is not with the technologies per se but rather with the conditions under which growth flourished. Thus, he explains that the French lagged behind the British in steel production and the adoption of new steel technologies in the early 18th century chiefly because the French refused to use anything but French iron ore for reasons of national pride. The British had no such obsession with local content

and were satisfied to use imported iron. He shows how the rulers of two very dissimilar nations—Catholic Spain and Confucian China—followed similar paths in restraining learning and the dissemination of knowledge and thereby condemned their societies to slower growth. And he describes a work ethic and commitment to learning among Buddhist monks in 16th century Japan which Landes argues carried over to society at large: "One does not have to be a Weberian Protestant to behave like one," he concludes.

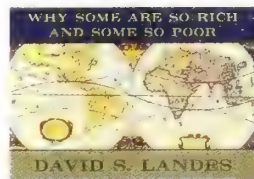
Landes manages to convey a great deal of information and in so doing, draws useful parallels between past and current events. It's impossible, for instance, to read his description of the importance of hydraulics as a symbol of political power to the despots of ancient China without thinking of the building of the massive Three Gorges Dam in today's China. Likewise, it is difficult to consider the benefits of the flexibility that medieval Europe's political fragmentation encouraged without considering how present-day Europe's ongoing economic union might diminish growth.

But for all its value as a rich source of information, *The Wealth and Poverty of Nations* falls short of its ultimate aim: to explain just why some are so rich and some so poor. Landes contends that culture, by which he means inner values and attitudes that guide a population, "makes all the difference." He rightly notes that culture is not a concept economists like, because it is inherently unquantifiable. And he says it frightens scholars because of its "sulfuric odor of race and inheritance." But then, he seems to contradict himself when he admits that culture adapts, and that culture alone does not determine outcomes.

In the end, Landes can do little more than extol an open, optimistic approach to growth, development, and indeed to life. It's a homiletic—and disappointing—conclusion to a fascinating and vexing study of economic history.

BY KAREN PENNAR
Senior Writer Pennar has written often about the debate over growth.

THE WEALTH AND POVERTY OF NATIONS



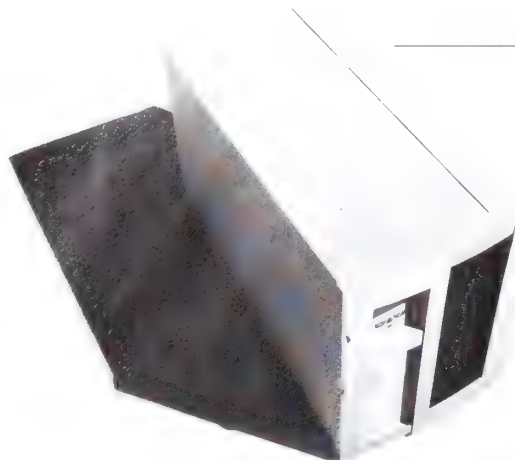
LANDES FALLS SHORT OF HIS MAIN GOAL: TO EXPLAIN WHY SOME ECONOMIES THRIVE



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BY STEPHEN H. WILDSTROM

THE PALMPILOT FLIES HIGHER

No longer just a techie toy, this handheld makes it easier to stay connected

I have been a fan of the PalmPilot ever since the "connected organizer" was introduced two years ago. Originally, the "connected" notion just referred to the way the PalmPilot made it extremely simple to exchange contact and calendar information between a PC and the handheld unit. Now, the PalmPilot can connect to the Internet or corporate networks—even by wireless.

The \$399 Palm III, introduced on Mar. 9, continues the evolution from techie toy to business tool. In addition to a sleek new design and more memory, the latest version can exchange information with other Palm IIIs via an infrared link. But the real growth of Pilot as a business communicator comes from an explosion of third-party software and accessories that enhance its ability to link up with corporate networks.

WEB DATA. One interesting new application for PalmPilots comes from startup AvantGo (650 638-3399). AvantGo lets you designate Web pages for download. When you hook up your Pilot to a PC, the contents of those pages are automatically copied onto your

handheld for viewing offline.

At first glance, this looks like a stupid idea, since a 5-sq.-in. monochrome display makes for a wretched presentation. But AvantGo is designed for business, not surfing. Its power becomes apparent when it is used to download data from an internal corporate Web server. For example, a company could set up a Web page containing daily product price and inventory data, formatted for optimal display. When field salespeople synchronize their PalmPilots with their PCs, they automatically get the new data. For many, this may eliminate the need for a clunky—and much more expensive—laptop. The AvantGo software is being offered at an introductory price of \$49 per copy, and a free trial version is available at www.avantgo.com.

Mobile users can't always get to their desktops to connect. So last year, Palm introduced a modem for the PalmPilot. The modem was fine—Palm's parent company, 3Com, is a huge modem maker—but the software, especially the E-mail, was clumsy. Improved software, such as the HandStamp E-mail program from Smartcode Soft-

ware (619 597-7544), is making remote communications a lot easier. Also giving that trend a big boost are a willingness by corporate network administrators to support PalmPilots, and now, wireless connections.

The Minstrel wireless modem from Novatel Wireless (619 784-0620) allows a Pilot to connect to the Internet using wireless technology called cellular digital packet data (CDPD). Although the \$400 Minstrel more than doubles the size and weight of the Pilot, the package is still smaller than a Hewlett-Packard 620LX handheld PC. Novatel offers national CDPD service, which runs over

The Minstrel-Pilot combination is useful mainly for sending and receiving E-mail on the run. While the PalmPilot isn't great for long messages, it handles short notes well. Once you have mastered its Graffiti shorthand, it can be easier to use to write messages than the mini-keyboards on other handhelds.

REAL-TIME QUOTES. Other services are starting to take advantage of this communications ability. For \$115 per month plus a \$100 activation fee, your Minstrel can receive MarketClip from Reuters (888 978-6257), which provides real-time stock quotes, charts, graphs, and market news for traders.

If you want a wireless connection with less bulk, the \$70 One-Touch cable and software from J Systems (972 484-5432) allows a Pilot to send and receive E-mail through a two-way pager from SkyTel or MCI (BW—Feb. 16). The combination takes advantage of the good coverage and reliability of the two-way paging network, while overcoming the clumsiness of reading and, especially, entering E-mail messages on a pager. If you are lucky enough to live in Wash-

ington, D.C., Seattle, or the San Francisco Bay area, you can get similar, but much faster, communications for \$349 plus \$29 a month using a Ricochet wireless modem from Metricom (800 469-4735).

Most Pilots are still used as simple organizers. But new communications options are giving these handy devices real clout as business tools.



THE PALM III WITH A DESKTOP ATTACHMENT (ABOVE) AND THE PALMPILOT WITH MODEM (LEFT)

the conventional analog cellular network, through GoAmerica. It costs between \$15 and \$100 a month, depending on the amount of data moved. Service is also available from some local cellular carriers. CDPD is available in most large metropolitan areas, but it can bog down at times when cellular traffic is heavy, such as evening rush hour.

New Linkups for the PalmPilot

	MANUFACTURER	FUNCTION	MAIN USE
AVANTGO	AvantGo	Downloads Web pages	Updating price list, other information
MINSTREL	Novatel Wireless	Wireless modem links Pilot to the Internet	E-mail, real-time delivery of financial market information
ONE-TOUCH	JP systems	Links to two-way pager	Wireless E-mail, mainly for short messages

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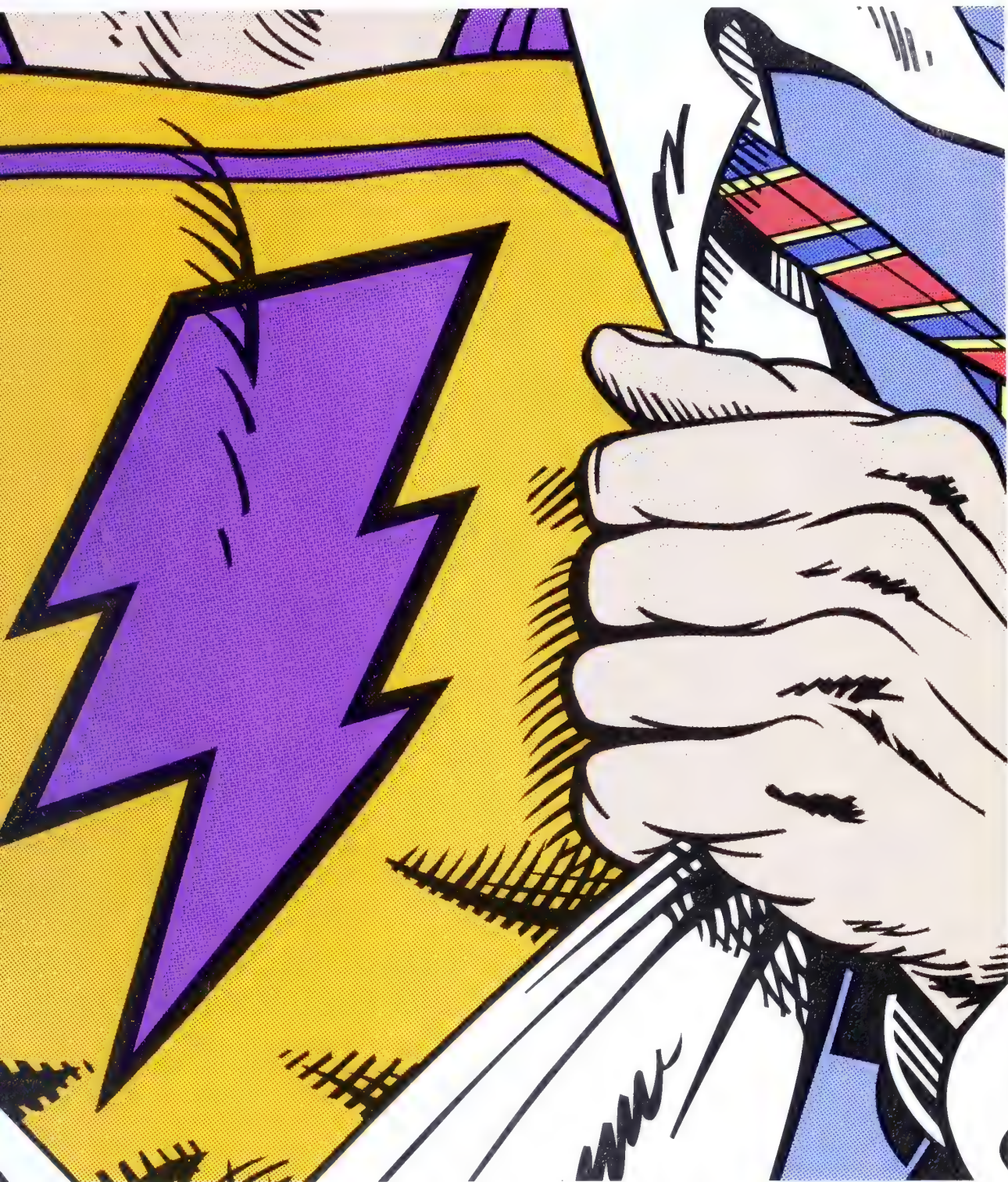
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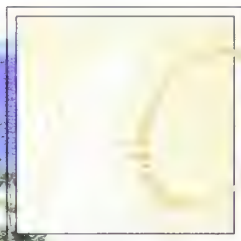
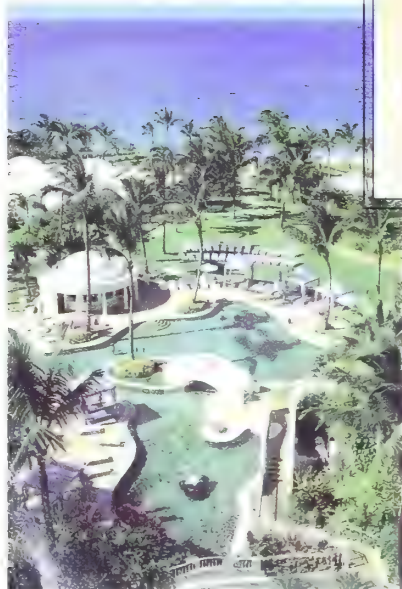
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JEFFREY E. GARTEN

WHY THE GLOBAL ECONOMY IS HERE TO STAY



THE WORLD:
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y links
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onomies are
breakable

Twice before in this century, globalization seemed to be the wave of the future. In the two decades before World War I, international flows of money were tying Europe ever closer to America, Asia, Africa, and the Middle East. Stock markets were booming on both sides of the Atlantic, and banks and private investors were busily diversifying their investments from Argentina to Singapore. But by 1914, nationalism, bad economic policies, and war brought these trends to a brutal halt. In the 1920s, foreign investment and international commerce took off again. But soon, the factors that killed the first wave of globalization reemerged, shattering growing global linkages.

Is there something deeper and more durable about globalization in the late 1990s? Can this third attempt at globalization withstand the meltdown in Asia, sky-high unemployment in Europe, stubborn poverty in Latin America, and soaring trade deficits in the U.S.?

You bet. War is remote, and central bankers have learned a lot from their mistakes. Today, globalization has become a permanent and irreversible part of economic life. This is not just because of the phenomenal growth of world capital markets reflected in the power of a Merrill Lynch & Co. or a George Soros. More important, by far, is the integration of the latest information technology into corporate strategies. Globalization is different in the 1990s because it is being driven by the first truly global companies.

Federal Express Corp. both epitomizes this trend and is a major force behind it. Delivering some 2.8 million packages in 210 countries each day, FedEx is pushing globalization faster and deeper, not just because it is adding more planes and routes but because it is using information technology to reengineer its clients' worldwide supply and distribution systems. In the process, global sourcing and sales are becoming an ever more integral part of these companies' way of operating.

Indeed, FedEx has become the global logistical backbone for many of its corporate customers. It manages their worldwide inventory, warehousing, distribution, and customs clearance, using state-of-the-art technology. It can help a client assemble and make products with near-perfect precision by securing supplies from Penang to Peoria in the most reliable and cost-effective way, while

squeezing unnecessary mass out of expensive inventories.

FedEx can perform these functions because it can electronically track where any shipment is at any given moment, and it can guarantee on-time delivery. Clients feel comfortable reducing inventories, which they previously held in large quantities as insurance against the variability of delivery. For many companies, it's a short step from that to working with FedEx to plan their entire global supply systems.

The core of FedEx' global strategy is to use information technology to help customers take advantage of international markets. In fact, FedEx sees itself more as an information-technology company than as a transporter of goods. Today, more than two-thirds of FedEx customers handle orders and deliveries online. "We decided years ago," says Chairman and CEO Frederick W. Smith, "that the most important element in this business is information technology, and we have geared everything to that philosophy—recruitment, training, and compensation. Fail-safe precision is the key to it all."

FULL SERVICE. One of FedEx' oldest and most far-reaching supply-management relationships is with National Semiconductor Corp., which has facilities in the U.S., Europe, and Asia. FedEx manages its global warehousing and distribution systems, reducing National Semi's total logistics cost from 3% to 1.9% of revenues between 1993 and 1996. Another example is Dell Computer Corp., which has eliminated its costly distribution infrastructure and relies on FedEx to coordinate the assembly of computers and their customs clearance and shipping from a manufacturing center in Malaysia to customers in Japan and Taiwan.

The marriage of information technology and transportation is a major reason that links among national economies have become so much tighter. In past phases of globalization, governments were the driving force, lowering trade barriers and stabilizing currencies. Today, the pressure to make the world one market is coming less from capitals than from companies. International corporate linkages are becoming resistant to occasional flare-ups of protectionism. In fact, what FedEx illustrates is not only that today's globalization is qualitatively different from its predecessors but also that it is now truly irreversible.

Jeffrey E. Garten is dean of the Yale School of Management. A former investment banker, he was Under Secretary of Commerce for International Trade in the first Clinton Administration. (jeffrey.garten@yale.edu).



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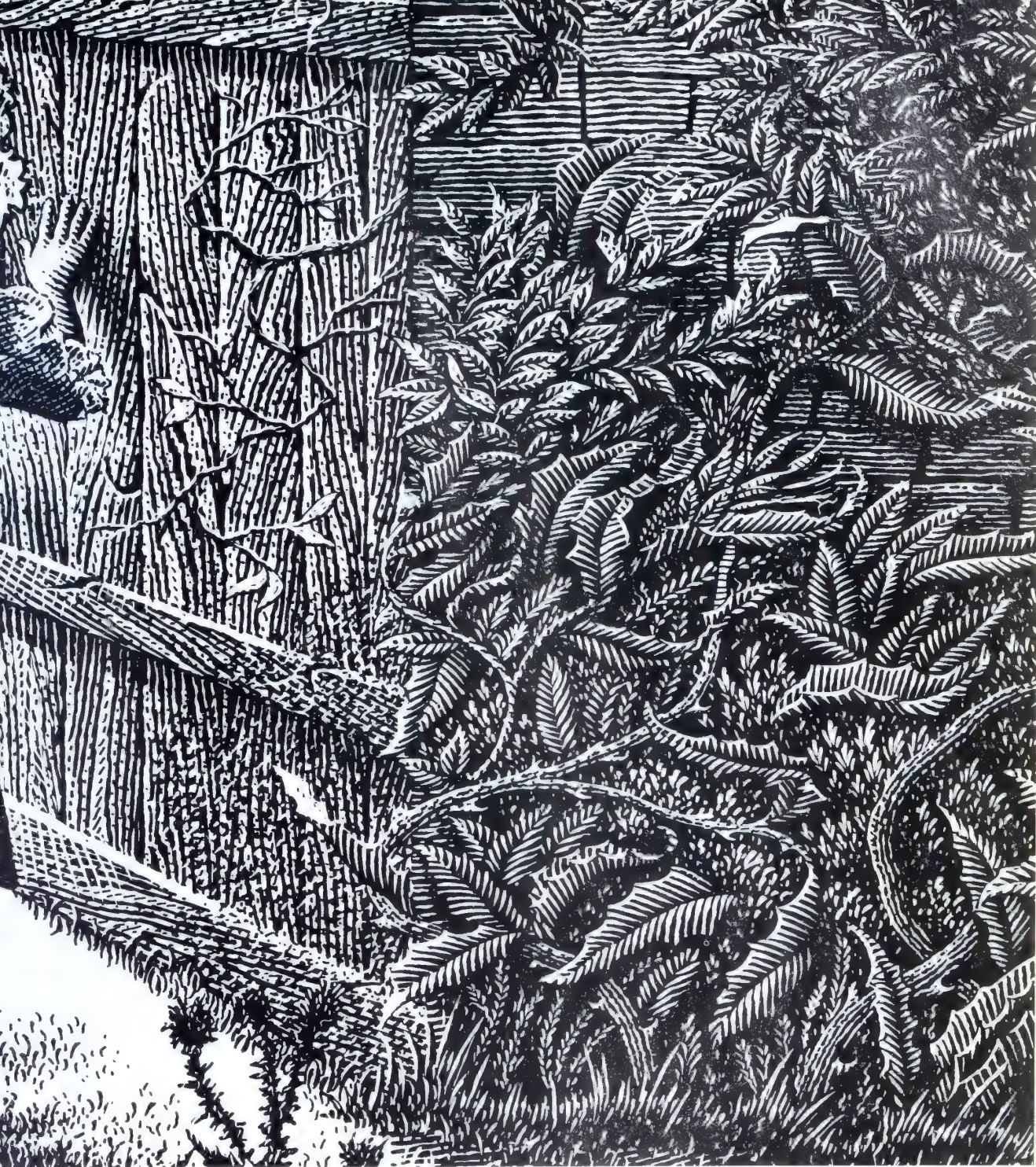
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HOW NOT TO FIX SOCIAL SECURITY

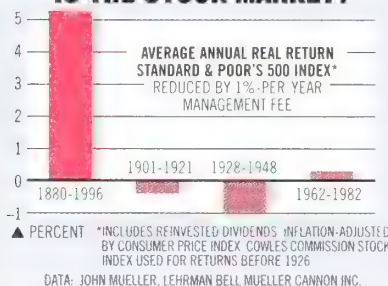
Stocks are too risky for retirees

For those who believe that Social Security should be privatized, the times could not be more propitious.

On the one hand, Bill Clinton has responded to widespread public anxiety by vowing to save the system so that future benefits are secure. On the other, the stock market remains buoyant after doubling in just three years. So it's no surprise that some Social Security critics are pressing harder than ever for reforms that would permit workers to invest a healthy chunk of their payroll taxes in stocks via individual accounts.

One economist who demurs is John Mueller of economic consultant Lehman Bell Mueller Cannon Inc. Writing in

JUST HOW DEPENDABLE IS THE STOCK MARKET?



Challenge magazine, he argues both that the stock market is too risky to depend on for retirement income for most people and that it is likely to underperform in coming decades.

Mueller concedes that stocks have produced an average real annual return of about 6.2% since 1880 (5.2% if one subtracts a 1% yearly management fee), whereas future retirees can expect an inflation-adjusted return of only 1.4% or so on their Social Security contributions. But he notes that such positive returns were far from steady. Indeed, the market has posted annual declines about a third of the time since 1900.

Moreover, these drops were not random but tended to occur in three 20-year periods: 1901 to 1921; 1928 to 1948; and 1962 to 1982. Mueller calculates that average annual real returns (including dividends, but minus management fees) during these periods were either negative or less than 1%. Their 20-year du-

ration is significant because most families only save big for retirement in the last two decades of their working lives.

What this means is that someone who invested in stocks and then retired during one of these periods stood a strong chance of winding up with little or no gain in inflation-adjusted terms. By contrast, investors lucky enough to retire in other periods could have racked up real average gains of as much as 10% a year.

Mueller's point is that this degree of risk, which could hurt a generation of retirees, is too high compared with the small but secure real return projected for Social Security. Further, he doubts that stocks will produce the large returns many experts anticipate.

One reason is that the market tends to perform badly when the number of middle-aged workers falls relative to young workers in their household-formation years. This will soon start to happen as the relatively small Generation X displaces baby boomers in the peak saving years and a larger group of echo-boomers (baby boomers' kids) enter their peak borrowing years. Stocks also may suffer when retiring boomers start liquidating their private pension savings.

Secondly, Mueller notes that Social Security's future woes are predicated partly on the assumption that future economic growth will slow sharply. But the stock market's fate also depends on economic growth, so it, too, would lag behind its historic performance. On the other hand, if productivity and economic growth prove stronger than projected, the return on Social Security contributions will rise, and the system will face far smaller problems.

"We need to restore Social Security's long-run solvency," says Mueller, "but privatization is not the answer."

THE STURDIEST SAFETY NETS

Two programs keep hunger at bay

A new analysis of the impact of government programs on poverty underscores the importance of Social Security to the elderly and of the earned income-tax credit to low-income children.

According to the Washington-based Center on Budget & Policy Priorities, Social Security alone lifted 37% of the elderly, or 11.7 million seniors, out of poverty in 1996—nine times as many as all other government support programs, including such noncash benefits as food stamps and housing assistance. It also

kept an additional 4.3 million adults and children, mainly disabled workers or dependents of deceased workers, from falling below the poverty line.

Meanwhile, the Earned Income Tax Credit, which supplements the wages of low-income working families, has emerged as the largest single program to ameliorate child poverty, accounting for 37.3% of the 5.3 million children moved out of poverty by all government programs in 1996. Overall, however, the center notes that the number of children lifted out of poverty fell by 400,000 in that year, partly as a result of the improving economy but mainly because of cutbacks in other government support programs.

LIFTING AMERICANS OUT OF POVERTY

PERSONS RAISED FROM POVERTY IN 1996 BY:

SOCIAL SECURITY

NUMBER IN MILLIONS	
ELDERLY	11.7
OTHER ADULTS	3.5
CHILDREN	0.8
EARNED INCOME TAX CREDIT	
ADULTS	2.2
CHILDREN	2.4
DATA: CENTER ON BUDGET & POLICY PRIORITIES	

POTENT FUEL FOR SPENDING

Mild weather and early tax refunds

Last year, warm weather and early tax refunds spurred consumption in the first quarter. That seems to be happening again this year.

As economist Joseph T. Abate of Lehman Brothers Inc. notes, average temperatures in January were 16% above normal, and February and early March seem equally mild. The strongest components of retail sales in recent months, he adds, have been the most weather-sensitive: hardware, garden items, apparel, and general merchandise. Meanwhile, increased electronic filing boosted tax refunds in January and February by \$3.1 billion over last year's receipts and \$10 billion over the take in 1996. Since refunds usually hit their stride in March, consumers could have even more of the green stuff to spread around this month.

The big question, however, is what happens in April. Last year, households were hit with a hefty \$122 billion tax bill in that month, which helped brake spending sharply in the second quarter. If it happens again, some experts think the current spending juggernaut could lose a lot of its pizzazz.

MES C. COOPER & KATHLEEN MADIGAN

READY TIMES FOR WORKERS, HARD TIMES FOR COMPANIES?

Real wages are outpacing productivity—and profits are at risk

U.S. ECONOMY

Ho-hum. Another unexpected-ly strong report on the boom- U.S. labor market, and another yawn from Wall t. It's a reaction that would have seemed impos- a few months ago.

w, though, the bond market isn't worried that uary's surging payrolls, tight job markets, and e wage growth will cause the Federal Reserve to nterest rates, as long as the Asian crisis keeps the mny from overheating. And the stock market, n nervous about the tech sector, seems to think that labor costs amid little pricing power is no great t to profits. It seems as if nothing can crack Wall t's tough veneer.

be sure, the outlook for inflation overall in 1998 is good, thanks to the effect of Asia's collapse on the g dollar; the ensuing weakness in commodity prices ally, and the sharp drop in oil prices in particular. r materials costs will also help the bottom lines of businesses at a time when profit growth is slowing.

THESE ARE GOOD TIMES FOR WORKERS



PERCENT CHANGE FROM A YEAR AGO
HOURLY EARNINGS DIVIDED BY
PRICE INDEX FOR CONSUMER SPENDING
*LABOR DEPT. BUSINESS WEEK

paying out increases in real wages in excess of advances in productivity without seeing their margins suffer.

fact, the crucial determinant in the 1998 outlooks profits, inflation, monetary policy—and Wall Street—be the success of U.S. corporations in managing labor costs. And judging by the February report the labor markets, companies have their work ut for them.

ONLY DID JOB GROWTH

continue to be nothing of phenomenal in February but the unemploy- rate also dipped back to a 24-year low of 4.6%, 4.7% in January. And there is every reason to be- that it will go lower. At the growth rates of em- ment and the labor force during the past six months,

the jobless rate would fall below 4.5% by summer.

But the biggest surprise last month was another large gain in payrolls, which rose by 310,000. Jobs in the service sector continued to lead the growth, al- though strong homebuilding, coupled with mild weath- er and cleanup efforts after flooding and ice storms, boosted construction employment. During the past four months, job growth has averaged 367,000 net new hires per month, the most for any such period since 1984. And in the past half-year, jobs have increased by 2 million (chart).

Amid continued pressure to find workers, compa- nies increased the average hourly wage rate by 0.6% in February, to \$12.60, and pay in the service-producing industries increased by an even greater 0.8%. Those ad- vances lifted the annual clip for overall wages to 4.1% from a year ago, and service-sector pay is rising at a 4.5% pace. Adjusted for inflation, using the chain- weighted price index for consumer goods and services, real wages are up 2.9% from a year ago, the fastest pace since 1974.

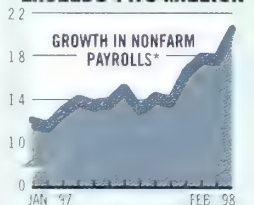
GAINS IN REAL PAY

have further to run this year. With the domestic economy so strong, labor markets are almost certain to remain very tight. Not only will pay gains continue to pick up, but with inflation set to remain low, any addition to the pace of pay will trans- mit immediately into real wage growth.

In particular, lower oil prices have already provided a sizable anti-inflation impact, which should continue this year. Cheaper oil cut 0.2 per- centage points from the 1997 inflation rate, and the 1998 impact could be twice that. Crude prices fell from more than \$26 per barrel at the end of 1996 to \$18 at the end of 1997. So far in March, prices have dropped below \$15, a four-year low, with further declines likely. OPEC continues to produce be- yond its quota, and the collapse in Asian demand has created a worldwide glut that will not be soaked up anytime soon.

Of course, if businesses are getting 2.5%-to-3% pro- ductivity growth from their labor, then real wages can rise that fast without squeezing profit margins. There's

SIX-MONTH JOB GROWTH EXCEEDS TWO MILLION



▲ MILLIONS OF WORKERS
*CUMULATIVE GAINS OVER SIX-MONTH PERIODS
DATA: LABOR DEPT., BUSINESS WEEK

Business Outlook

the rub. Productivity growth in the past two years has averaged a stellar 1.9% annually, but even at that pace, it has started to fall behind real pay gains, and it may well stay behind throughout 1998.

Nonfarm productivity growth in the fourth quarter of last year was revised down from a 2% annual rate, to 1.6%, but even that healthy pace could not prevent unit labor costs from rising at a 3.5% annual rate. That's because fourth-quarter compensation jumped 5.2%, the most in any quarter in nearly six years.

Moreover, based on labor market data through February, unit labor costs appear to have increased even faster in the first quarter. Hourly pay in the first quarter is rising at an annual rate of 4% through February. Meanwhile, hours worked are on a track to rise at an annual rate of about 5.5%, which should swamp the likely growth in output. That means there will be little if any gain in productivity to prevent higher pay from feeding directly into unit labor costs.

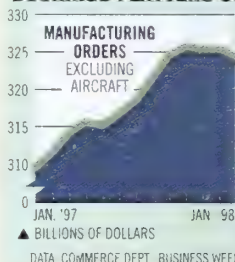
THE HOPE ON WALL STREET is that Asian weakness will cool off overall demand, thus easing labor market pressures. But so far, there is no evidence of that. Clearly, softer Asian demand is showing up in the manufacturing sector. Factory orders rose 0.5% in January, bouncing back from a December drop caused by a swing in aircraft orders. But the trend in bookings excluding planes has fallen off in recent months

(chart), in tandem with signs of weaker export orders. Moreover, the February employment report showed that manufacturing payrolls dipped slightly, after four months of solid gains. Also, the factory workweek, often a leading indicator of employment, declined for the second month in a row. Factory production, while growing more slowly this quarter, compared with the fourth quarter's 8% annual rate, still appears to be increasing at a moderate pace of about 4%.

But because the overall labor market remains so strong, consumers are leading unrelenting strength in domestic spending, especially in services. In turn, intense demand for labor continues to fuel real wages—and even more spending. The outlook for 1998 may well turn on how this virtuous cycle plays out.

The most likely scenario: As long as businesses lack pricing power, this cycle is self-limiting. That's because profits will get squeezed. Capital spending will suffer. Employment will slow, and the economy will cool down on its own. So if you're a worker, enjoy the good times while they last. But if you're an investor, you should worry that those good times might come at a hefty cost to Corporate America.

THE TREND IN FACTORY BOOKINGS FLATTENS OUT



UKRAINE

UNDER THE GUN IN KIEV

American Secretary of State Madeleine K. Albright carried a blunt warning on a Mar. 6 visit to Kiev: Unless the pace of economic reform picks up, the U.S. could halve Ukraine's \$225 million aid package this year. That's a troubling prospect—but hardly the only one looming on Ukraine's horizon.

While most of its neighbors in the former Soviet bloc are poised for growth, Ukraine's darkest days may lie ahead. After contracting by two-thirds since 1991, the economy shrank another 0.8% in January, with a sharp 11.8% decline in industrial production. Practically none of Ukraine's rich agricultural and industrial base has been pri-

vatized. Foreign direct investment is \$39 per capita, one of the lowest figures in the region. And lack of privatization revenue contributes to a mounting budgetary crisis.

Aid donors are turning up the heat. The International Monetary Fund says it won't release a long-awaited \$2.5 billion loan without government action on fiscal and monetary reforms. The U.S. is urging relief from a corrupt regulatory regime that discourages investment and pushes some 50% of economic activity onto the black market.

Government borrowing is another time bomb. For the past two years, Treasury bill proceeds helped cover budget deficits. But

foreign investors fled after last fall's Asian meltdown. Now, with an estimated \$3.5 billion in redemptions due this year, Kiev is issuing Eurobonds. But to attract investors, it is forced to offer yields of 15% to 16%, far above the rates paid by most emerging-market borrowers. With parliamentary elections on Mar. 29, analysts fear the government could dig itself in even deeper by using Eurobond proceeds to start paying off more than \$2 billion in overdue wages and pensions.

Ukraine's currency, the hryvna, can't take much more of this. Last fall, the government propped it up by raising interest rates and dipping into reserves. But reserves are now below \$2 billion, and devaluation could soon be added to the list of Ukraine's woes.

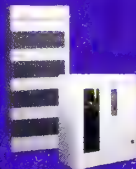
By Carol Matlack in Kiev

STILL STUCK IN REVERSE





It is beyond rich.
It represents a
gigabyte of data
poured into a network
that's spread across
corporate headquarters,
four manufacturing facilities
and 200 global sales offices.
But without the right storage
system in place, the taste it
leaves in your mouth is less
than desirable. Call StorageTek®
at 1-800-STORTEK or visit us on
the Web. Because when information
is a critical ingredient in your
business, you should consider
partnering with a company that
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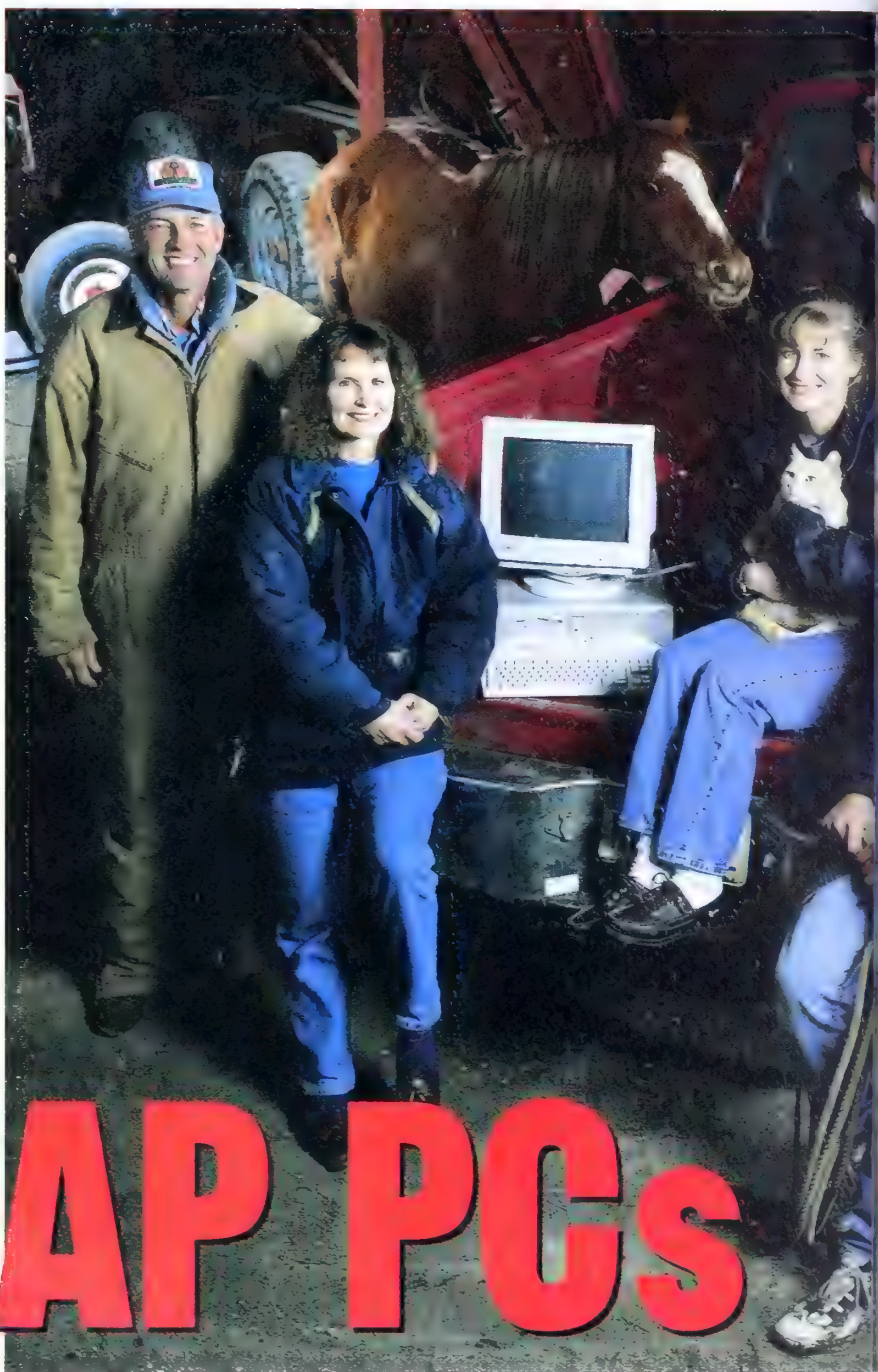
Where the world's information goes.

The Model Ts of the Digital Age will help wire the world. But will they bring prosperity to computer makers?

For years, Gerald Busenitz refused to buy a personal computer. The 49-year-old owner of an 1,800-acre farm in Newton, Kan., told his disappointed son that he would just have to keep doing his homework on a PC at school—the family couldn't justify \$2,000 for a machine he didn't even know how to use. "If I buy a tractor, I can make the farm more profitable," he told his wife, Margie. "But a PC? I just couldn't see it."

He can now. On Mar. 2, the Busenitzes took the plunge, bringing home a Compaq Presario—for \$999 including a monitor. "I think the price has gotten to be about right—plus, we had a good year," says Busenitz.

That's just what executives at Compaq Computer Corp. had hoped would happen last spring, when they redesigned Compaq's low-end home PCs and cut price tags to below \$1,000. Oth-



CHEAP PCs

er PC makers quickly followed, and by yearend, sub-\$1,000 PCs accounted for 30% of all computers sold through U.S. computer and electronics stores. A third of those sales were to people who had never before purchased a PC.

UBIQUITOUS. In short order, the flood of new buyers nudged the penetration of PCs to 43% of U.S. homes—up from the 40% range where it had been stalled for three years, according to IDC Link. From January, 1997, to January, 1998, the average selling price of a home PC dropped 30%, to \$1,169. By Christmas,

1998, analysts expect top PC makers to offer \$600 machines—setting the stage for PCs to find their way into 60% of U.S. homes by 2002, according to projections by Forrester Research Inc.

If those numbers prove accurate, the home-PC business is in for at least several more years of steady growth—from 12 million units a year now to 17.5 million by 2002, figures Forrester. And

American society will be in for another profound change at the hands of technology. Why? Because the PC will no longer be simply a staple of white-collar households, but a nearly ubiquitous tool for most Americans—like the telephone or the automobile. Even now, the new cheap PCs are bringing blue-collar families into the Digital Age. According to a survey by Forrester, the median income

The median income of people intendin

DIGITAL HARVEST: *The Busenitzes, Kansas farmers, finally took the plunge: a \$999 PC*

of people intending to buy such PCs is \$27,000, vs. \$50,000 for current PC owners. That means that the electronic realms where home-PC owners roam will be opened to millions more citizens—to shop, to chat, and to explore.

The new online masses are apt to bring huge changes to the Web—and perhaps new riches for people doing business there. Indeed, investors are already bidding up shares of companies such as Yahoo! Inc. and Excite Inc. on the assumption that the millions of consumers snapping up cheap PCs will bring more traffic to those Web sites—driving up ad rates and generating many more transactions. Electronic commerce could quickly change from a bonanza for the few—such as Amazon.com—to a huge business for all sorts of online merchants.

But the arrival of the new mass-market computer heralds painful changes for companies that make PCs. While the number of PCs sold through U.S. stores grew 54% for January over last January, revenues grew a measly 10%, says Computer Intelligence.

There's a parallel in the corporate computer market: the cash cow that enabled companies such as Compaq to compete so hard on PCs. Watching prices contract in PCs, machines not vastly different from what they use, corporations have added price cuts, too. In 1998, prices on all kinds of corporate hardware, from servers to notebooks, are expected to drop as much as 20%. James D. Poyner

Jr., an analyst at Oppenheimer Securities, estimates that profit margins on corporate PCs will drop to the low teens, close to the single-digit margins on some home PCs. When the year is over, predicts International Data Corp., computer makers around the world will have shipped 13.4% more PCs. But thanks to price cuts, their revenues will be up only 4.4%.

PRICE WAR. That means a profit pinch ahead and the casualties are already mounting. On Mar. 6, Compaq announced that its first-quarter sales had fallen short of its optimistic forecast. Revenue, it warns, will likely be flat with last year's final quarter, at about \$7.25 billion, and profits are likely to drop 25% for the year—to \$1.4 billion. On Mar. 4, Intel Corp. stunned investors by announcing that first-quarter sales would fall 10% below the fourth quarter's, its worst quarterly revenue drop in a decade. And Intel is expected to post its first year-over-year profit decline since 1989. Analysts think it will earn \$5.9 billion, down 15% from 1997's record \$6.5 billion. One factor affecting the chip giant: the inroads made by the likes of Advanced Micro Devices Inc., whose inexpensive Pentium clones go into the new cheap PCs.

As often happens, there's a momentary pause in final demand as buyers await lower prices. The PC industry knows what to do now: stage a price war. "We've been at the

edge, and it seems we just jumped over," says Oppenheimer's Poyner. "The question is whether the industry jumps back."

Indeed, this year's jolt may be anything but routine. Increasingly, PC makers are bracing for a fundamental change in their industry—a wrenching shift to a new, lower-margin business model. They will, most likely, come to resemble the consumer-electronics com-

panies with whose products theirs are increasingly in competition.

When the dust clears, the personal computer will have morphed into a true mass-market phenomenon—the Model Ts of the Digital Age. Just as Henry Ford's car for the masses profoundly changed where and how Americans lived, the next generation of low-priced computers will revolutionize the computer industry, the Internet, and lifestyles. With personal computers in 60% of homes, for example, the number of Americans surfing the Web could explode. Assuming it gets easier to use, "the impact could be as great as

the impact of the TV," says Paul Saffo, director of the Institute of the Future.

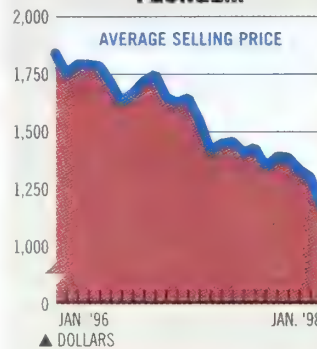
Already, you can see the beginning of the revolution. Cheap PCs will make Web-surfing, electronic learning, and digital commerce so much a part of daily life that many families will have multiple PCs. In a recent BUSINESS WEEK/Harris Poll of 1,009 people, 25% of those who bought a PC last year were adding one to their home.

But price alone will not put the personal computer on a par with cars, phones, and TVs in the lives of Americans. "We're doing what we need to do to move to 60%," says Microsoft Chairman William H. Gates III. But reaching the 36% of Americans who still say they see no need for a PC will require more than cosmetic changes and low prices. "As the price

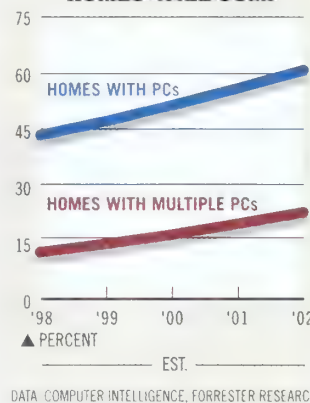
drops, computer manufacturers are forced to get volumes up," says Arno A. Penzias, a Nobel prize-winning physicist who is now chief scientist of the Bell Laboratories unit of Lucent Technologies Inc. "The only way to do that is to make things less intimidating. The real winners are people who can make these things look friendly."

Computer makers and folks who build

AS HOME PC PRICES PLUNGE...



...PENETRATION INTO U.S. HOMES WILL JUMP



DATA: COMPUTER INTELLIGENCE, FORRESTER RESEARCH

cheap PCs is **\$27,000**, vs. **\$50,000** for current PC owners



CONSUMER TOOL: consumer-PC chief
A mass-market Webb McKinney.
PC must work as So, ironically, 19
easily as a TV years after Apple
Computer Inc. se

out to build "a computer for the rest of us" with the easy-to-use Mac, it may be up to Intel and Microsoft to finish the job. These companies have the profits to fund research and development for the industry and are starting to do so. Since 1996, Intel has invested some \$450 million in startups pushing the edges of multimedia, videoconferencing and Web content, and now it is attacking the consumer-PC market more directly. On Mar. 4, it announced it will develop a separate microprocessor family, called Celeron, aimed at the low end consumer market. Intel's push: to make the PC better at handling visual information. Intel, says Chairman Andrew S. Grove, won't "make compro-

the technology that go into them are paying close attention. If PC makers don't do it, somebody else will. "All I want to do is send E-mail and access Web sites," says Robert Anderson, a West Palm Beach (Fla.) nurse, who recently passed up a home PC and bought a \$199 WebTV setup. He's one of 250,000 customers for the service that lets you surf the Net via TV. "I don't want to worry about all those icons and stuff," he explains.

But how can PC makers, whose margins are shrinking—perhaps permanently—fund development of innovative products? They can't. Those that can-

The market share of the top five P

tried have pulled back. Compaq collaborated with Mattel Inc.'s Fisher-Price on PC add-ons for kids and with Thomson Consumer Electronics on a deluxe TV-PC combo. Neither project bore fruit. And now, with a new price war beginning in the sub-\$1,000 market, most computer makers are riveted on more immediate goals. "We don't want to go pioneer new markets when we're in share-gaining mode for the next two to three years," says Hewlett-Packard Co.

mises that will make that [PC] interface less friendly."

Microsoft says its main focus this year is on simplifying its software. That starts with Windows 98, due out in June. The plan is to tightly integrate its Internet Explorer browser with the Windows operating system, making the now-familiar browser format a fundamental way of using all kinds of computer functions. The company plans similar integration for its Windows N-

A WONDERFUL DAY IN THE CYBER-NEIGHBORHOOD

Three years ago, the Newton Street Elementary School in Newark, N.J., tried an experiment. Using federal grants, teachers sent PCs home with 15 students. They knew the kids would pull lots of information from the Internet, but never guessed how much the children would soon give back.

Within months, says program director Angela Caruso, the families, and their school were linked in a network with neighboring universities and hospitals. Chat rooms sprang up where students discussed health issues with doctors. Families caught up in the AIDS scourge banded together online. One girl who witnessed a drive-by slaying posted a poem so powerful that it galvanized an antigang movement. In a way that was utterly new, says Caruso,

"we created a close-knit community."

Newton Street is part of a great technology migration, which plummeting PC prices are sure to hasten. As it gathers force, the terrain in at least some stretches of cyberspace will finally start to look a lot like America. In a survey of 120,000 North American homes, Forrester Research Inc., based in Cambridge, Mass., found that almost 70% of new PC buyers will have incomes of \$50,000 or less. African-Americans and Hispanics who don't already own a PC are 50% more likely to buy one in the coming year than non-minority Americans who don't. In a matter of years, predicts Forrester analyst Bill Bluestein, "the concern about PC haves and have-nots will fade away."

Early Internet users, most of them

wealthy, white, and male, will probably groan about the latest hordes of "natives" flooding into cyberspace. Instead, they should applaud. Experiments as Newton Street's prove that access to computer technology can lift spiritual barriers between people, and transform lives. The technology "gives people a window," says Assistant Secretary of Commerce Larry Irving, whose office funds the Newark project. "The Net is a place where you can start to talk to your neighbor."

MORE CRIME. Irving has dozens of examples. Native Americans use the technology to preserve their language. Seriously ill kids in Mississippi hospital stay in touch with classmates over the Net. Shopowners in eastern Kentucky sell crafts online. And in working-

ork operating system, which is due y early '99. Microsoft also hopes to to make desktop PCs behave more y sets—easy to use and quick to on and off. That means no “booting and an end to maddening software es. “Can you imagine if your TV ed when you tried to change chan-’ asks Paul Voois, chairman of phone maker 8x8 Inc.

ore the PC is reinvented, though, dustry may have to revamp how s business. Already, Wall Street sts are making massive downward ons on their earnings estimates ompaq, Micron Electronics, IBM, P. Some analysts think PC mar- may keep eroding to the range of mer electronics. That means even er pressure on manufacturers to prices and build market share.

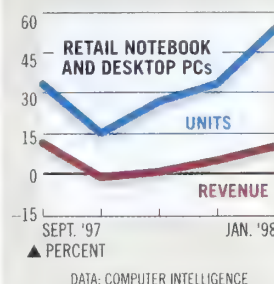
vitably, the result will be more y consolidation. Analyst Vadim otnikov of Sanford C. Bernstein & gures the top five players com- a 10%-to-13% cost advantage on

ing demand. But rivals and computer distribu- tors say much of Com- paq's problem stems from special deals that the PC leader offered to get them to increase orders.

“LIKE A DOG.” Mean- while, IBM may have even more PC products sitting on dealers' shelves than Compaq. IDC ana- lyst Jay Bretzmann says IBM has an eyebrow-raising 40 weeks' worth of PC servers in the reseller channel. Com- paq has 16 weeks' worth, and HP some 10 weeks'—both closer to typical levels for these products. Wall Street expects bloated PC inventories to cut into first- quarter earnings, which IBM has already signaled could fall 10% below last year. IBM declines to comment.

The result: Compaq and IBM will clear out inventories by slashing prices. That's going to put even more heat on sec-

SELLING MORE NOW, BUT ENJOYING IT LESS



customers to trade up to more powerful—and profitable—models any- time soon: There's no new software to overtax today's inexpensive but speedy Pentium ma- chines. Existing PCs will run Windows 98 just fine, and Microsoft's industrial- strength Windows NT 5.0 won't be out until 1999. “An 18-month-old PC may seem like a dog, but that's still a pretty nifty

machine,” says U S West Chief Infor- mation Officer David R. Laube. “It can certainly think a lot faster than I can type.”

That means computer makers must adjust costs now or wither. The No. 1 cost-efficiency mantra is death to in- ventory: by letting resellers assemble computers as orders come in from cus- tomers, PC makers can limit the amount of inventory in stock and get it sold

ers will rise from **34%** in '96 to an estimated **46%** in '98

components over smaller rivals. The top five—Compaq, Packard-Bell, HP, and IBM—will increase their com- market share from 34% of PC in 1996 to an estimated 46% in '98, he says, elbowing out AST Re- na, Acer, and Apple.

unt on a continuing drive for mar- share among the leaders. Never that a failed market-share grab Compaq's first-quarter woes. Offi- the company blames disappoint-

ond-tier players, already feeling the pinch of the new bargain-hungry PC buyers. Toshiba and AST left the home- PC business last year. Even IBM, which lost \$300 million on its consumer PCs in '97, is growing weary. “We're not particularly interested in chasing a lot of volume in businesses where we can't make money,” says IBM CEO Louis V. Gerstner Jr. “We'll be in the consumer- PC space, but we'll be there selectively.”

There's not much hope for getting

faster, before prices fall. Yet while Com- paq and IBM intend to use such tactics, they'll still be far behind direct-sales juggernaut Dell Computer Corp. The build-to-order king, whose costs are roughly nine percentage points less than rivals, continues to roll along. Michael Kwatinetz of DMG Technology Group ex- pects Dell to post a 50% jump in profits, to \$294 million, on a 49% rise in sales this quarter.

That leaves PC makers looking for



THAT'S PHAT!

People in all walks of life—from inner-city schoolkids to AIDS patients—are buying PCs, going online, and forming new digital communities

Alto, Calif., in Silicon Valley, kids produce a chat-style “for America Online. at migration won't be cost- ds in cyberspace spell worse

traffic jams at popular Web sites. With- in a year, expect to see tiered service on the Net: Folks who pay higher ac- cess fees can cruise the fast lanes, but not the disadvantaged.

In addition, even at \$20 a month, ac- cess fees will be a barrier for some, says Mercedes Soto, 30, who runs a program that promotes PC use at pub- lic-housing communities in Hartford, Conn. She also wonders who is going to train all of America's new PC users. Then, there's quality of life: A larger online community means more crimi- nals, more noise, and more confusion.

But Soto is optimistic that technology will be a force for good. Not long ago, she watched an 8-year-old at a project teach his parents how to get online. She came away less worried about training. A sense of community may also be the antidote to crime, says John Gage, top science officer at Sun Microsystems Inc. “The Internet should be like the best of cities. The streets are safe when a lot of people are looking out their windows.” With cheap computers, more people will share the view.

By Neil Gross in New York

new ways to make profits. One route is to broaden the line card with new products. The company that has cleaned up this way is HP, which has built a massive business selling PC printers and the ink and paper that go with them. It's unlikely that other PC makers can match HP's printer business, but, argues Poyner, they need to try to squeeze profits from non-PC

sales—things such as digital photo printers, videoconferencing gear, and hi-fi speakers.

Eventually, PC makers may have to think a lot bolder. "The railroads thought they were in the railroad business—until cars, buses, and trains showed them they were in the transportation business," says Antonio Perez, head of HP's printer business. "The PC

industry has a chance to remain the center of the home-computing universe." But only if PC makers realize that as much as they've changed the world so far, they now have to change themselves—and ultimately, the machine that got them here.

By Peter Burrows in Palo Alto, Calif. with Gary McWilliams in Houston, and Robert D. Hof in San Mateo, Calif.

BUSINESS WEEK/HARRIS POLL

AMERICANS ARE GETTING HOOKED ON THE HOME PC

The PC juggernaut rolls on—into home offices and family rooms everywhere. Of Americans who intend to buy a home computer in the next year, nearly two-thirds would be doing so for the first time, according to a recent BUSINESS WEEK/Harris Poll. Even better for PC makers, respondents expect to spend



an average of \$1,500 on the basic machine—\$2,400 with monitor, software, and accessories. Only 20%, in fact, expect the bill to be under \$1,000. Still the cheap PCs definitely have their appeal—especially as a machine for the kids and a tool to go online and do a little personal financial management.

AN UNTAPPED MARKET

Do you personally use a computer at home, work, or another location?

	USE	DO NOT USE		USE	DO NOT USE
Home.....	41%	59%	Another		
Work.....	44%	56%	location.....	24%	76%

THE TWO-PC HOME

If you use a computer at home, have you bought a computer in the past year?

Yes, have bought a computer	38%
No, have not bought a computer	62%

THE PRICE IS RIGHT

If so, how much did you pay?

	AVERAGE
Excluding monitor, software, and accessories	\$1,547
Including monitor, software, and accessories	\$2,300

IS IT YOUR FIRST?

Did the new computer...

Represent the first computer in your home?	34%
Replace an existing home computer?	41%
Add to an existing home computer?	25%

THE COMPUTER'S WINNING WAYS

How satisfied are you with your most recently purchased computer?

Very satisfied	73%	Not at all satisfied	0%
Somewhat satisfied	23%	Don't know	1%
Not very satisfied	3%		

IS THERE A PC IN YOUR FUTURE?

[All respondents] Do you intend to purchase a new home computer in the next year?

Yes, intend to purchase	27%
No, do not intend to purchase	71%
Don't know	2%

A FEW BELLS AND WHISTLES

If so, how much do you intend to spend?

	AVERAGE
Excluding monitor, software, and accessories	\$1,518
Including monitor, software, and accessories	\$2,399

NEWBIES ARE LEGION

Will the new computer...

Represent the first computer in your home?	62%
Replace an existing home computer?	24%
Add to an existing home computer?	14%

BARGAIN HUNTERS

If you have spent or intend to spend under \$1,000 for your new computer (excluding monitor and accessories), why?*

I don't need a machine that costs more than that	41%
I can't afford to spend more than \$1,000	37%
The new computer adds to an existing, more expensive computer that can do more	3%
Don't know	19%

THAT'S EDUTAINMENT

If you have spent or intend to spend under \$1,000 for your new computer, what will your new computer be used for? (multiple responses allowed)*

Kids' education and entertainment	41%
Personal finance management	38%
Internet/Web surfing	28%
Job-related work	26%
Entertainment	19%
Electronic mail	12%
Other	13%

EDITED BY KEITH H. HAMMONDS

Survey of 1,009 adults conducted Dec. 11-15, 1997, for BUSINESS WEEK by Louis Harris & Associates Inc. and the Baruch College of Business at the City University of New York.

*Because of small samples, caution should be used in interpreting answers to these questions.

Mitsubishi Has Shipped More Embedded DRAM Than All Other Suppliers Combined.



"eRAM"™ stands for "embedded random access memory" - Mitsubishi's brand name for its silicon process technology, products and systems expertise that integrate memory and system-level core functions in the same integrated circuit to enable unprecedented system performance. eRAM encompasses Mitsubishi's proven ability to combine memory - especially DRAM - microprocessor, and other logic core functions in a single piece of silicon. And, it's scalable across your product lines, which helps you save design costs and get to market faster.

Mitsubishi's HyperDRAM™ process technology and manufacturing

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ize an industry by "mobilizing multimedia". And it can do the same for

you. We've shipped over seven million embedded DRAM systems-on-

a-chip during the past three years*. That's more than all other suppliers

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COMMENTARY

By Michael J. Mandel

THE NEW ECONOMY STARTS TO HIT HOME

Is the New Economy making a big difference in the daily life of the average American? Not according to some skeptical economists and journalists, who argue that new products such as home computers and online services are inconsequential.

But these skeptics are wrong. There's a fundamental economic principle that states consumers spend their time and money in the ways that give them the greatest perceived benefits. To put it another way, if you want to know what's important to Americans, you need to watch what they do.

By that gauge, it would seem consumers are voting with their feet and their wallets for the New Economy. Spending on mainstays of the New Economy, such as computers and financial services, is up more than 12% over the last year, while purchases of old-economy goods like cars and clothes are barely rising. Moreover, many Americans are happily changing their daily routine to take advantage of the goods and services that define the New Economy—providing another piece of evidence that they see growing benefits from the technology on which the New Economy is founded.

Consider first the latest shifts in household spending. Over the last year, personal income has soared by almost 6%, while consumer confidence has jumped by 16% to a new record. In the past, that would have sent Americans scurrying into auto showrooms to buy either an additional car or a new model to replace an existing vehicle. Yet the latest report from auto makers, released Mar. 4, shows car and truck sales down 3.6% for the first two months of 1998.

COMPUTER BOOM. Instead, Americans are choosing to put the extra money in their paychecks into more computers. The number of personal computers bought at computer stores jumped by 54% from last January to this. Moreover, despite the sharp decline in computer prices, the actual dollars being laid out by households on computer gear is up 18% over 1997.

Other sectors also show the attraction of the New Economy for consumers. Despite a housing boom, sales of major appliances are up barely 1% over the last year. At the same time,

however, household spending on telephone services is up almost 9%, as more and more consumers order multiple lines and join up for cellular service. And instead of splurging on new clothing, investors are willingly paying brokerage and mutual fund fees in or-

der to ride the rising stock market.

Indeed, judging by their actions, Americans are enthusiastically availing themselves of the new options in financial services that technology is providing. Homeowners are quicker to refinance, in part because automated mortgage approval programs allow banks to grant mortgages faster and more cheaply. And, without today's powerful computers, it would not be economical to offer mutual funds and 401(k)s to the average worker. Also, though consumers say they resent the fees they now must pay at many automated teller machines, they keep using the ATMs—suggesting that the convenience and time-savings have real value.

HIGH-TECH TIMESAVERS. Sometimes new technology can be enticing enough to produce a very rapid change in behavior. For example, more than 60% of traffic on New York City's bridges and tunnels now uses EZ-Pass, a small radio transponder that allows people to pay their tolls without stopping. This level of acceptance, coming less than three years after EZ-Pass was introduced, points up the big gains: The resulting time savings for commuters—about 15 minutes a day, or more than 40 hours a year, allowing for holidays and vacations—is worth a week's wages.

Based on where consumers spend their money and time, even some seemingly frivolous uses of technology have real value. One of the most popular features of America Online Inc., for example, is its chat rooms, where people can argue, flirt, and generally mouth off. This may seem like a marginal enhancement to their well-being, but it's no more ridiculous than the notion of calling a friend on the telephone just to talk. What's more, AOL's 11 million customers value its services enough that the company was able to raise prices by 10% last month, something that car companies have been unable to do.

The truth is, in a market economy, value is determined by the preferences of consumers—and that's the way it should be.

Economics Editor Mandel has two computers and three telephone lines in his home.

CONSUMERS OPT FOR THE NEW ECONOMY

INCREASE IN PERSONAL SPENDING,
JAN. '97-JAN. '98

KEY OLD ECONOMY ITEMS

MOTOR VEHICLES

0.3%

FOOD

0.6%

MAJOR APPLIANCES

1.1%

CLOTHING

2.3%

AVERAGE

0.9%

KEY NEW ECONOMY ITEMS

HOME TELEPHONE SERVICES

8.8%

ENTERTAINMENT & RECREATION SERVICES

12.4%

CABLE TV

13.4%

BROKERAGE AND OTHER FINANCIAL SERVICES

15.6%

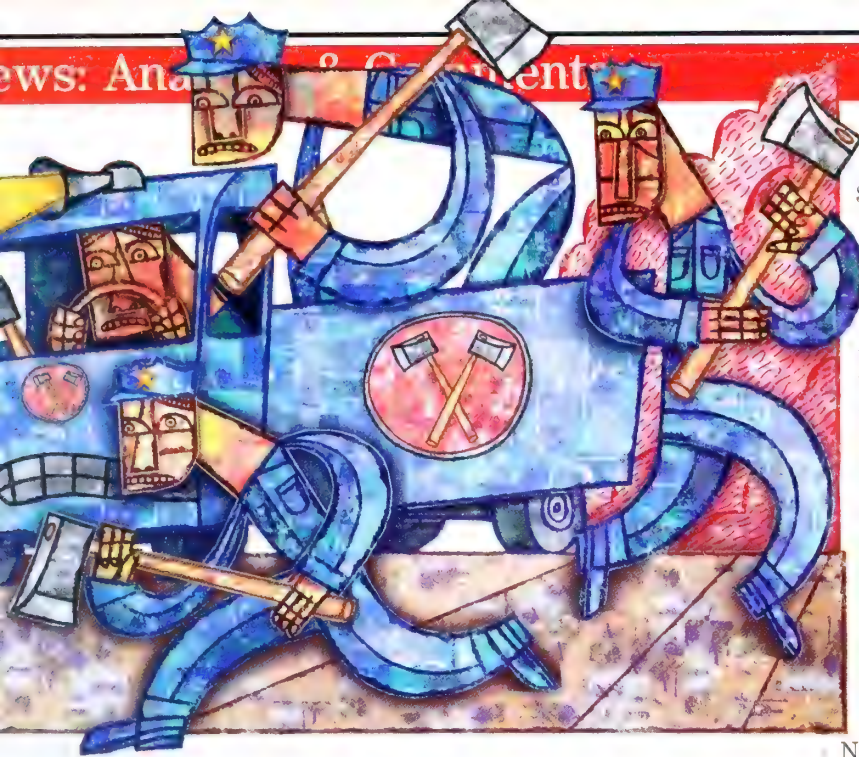
HOME COMPUTERS

18.1%

AVERAGE

12.5%

DATA: BUSINESS WEEK, COMMERCE DEPT.



STBUSTERS

AGAINST THE WALL, MONOPOLIST

Clinton's antitrust cops are getting so tough

months, WorldCom Inc. figured its record \$37 billion deal to buy MCI communications Corp. would sail through the Justice Dept. It figured it would. Turns out the antitrust division thought the megacombo could own more than half the communications lines carrying Internet traffic—and set unfair prices for rivals that need to hook on. It's the first case that defines "Internet competition," says William P. Barr, general counsel of GTE Corp., one rival. But it's not the first time that the trustbusters have staked out ground. And it won't be the last. WorldCom insists that its deal will even go through and that no one company can dominate the ultracompetitive Internet. Still, it's clear that the harsh move is a sign of change in Washington. After watching idly as massive consolidation rolled through industry after industry, the Justice Dept. and the Federal Trade Commission are launching a new antitrust offensive.

The reason for the new scrutiny: the merger mania. In 1997, antitrust attorneys reviewed 3,702 deals, up from 1,191 in 1991. To trustbusters, many of the best deals take consolidation just a step too far—into anticompetitive territory. "The message for Corporate Amer-

ica is that if you're in a consolidating industry, you want your merger to go through first," says New York antitrust attorney Kevin J. Arquitt.

Philosophy has as much to do with this newfound zeal as the economic landscape. FTC Chairman Robert Pitofsky and Justice's Joel I. Klein are big believers in government's power to fix market glitches, a major swing from their predecessors in the Bush and Rea-

NEW RULES "The message is, if you're in a consolidating industry, you want your merger to go through first," says one expert

gan Administrations. "There was a sense in the mid-1980s that antitrust enforcement should be minimal because the market would take care of most problems," says Pitofsky. "Enforcement today is more skeptical that the market will solve these problems. There are deals that will harm consumers."

Of late, the trustbusters have been working overtime to make their point. On Mar. 6, Justice officials told Lock-

heed Martin Corp. and Northrop Grumman Corp. that their proposed \$11.6 billion merger was in trouble. On Mar. 3, the FTC halted plans for four major drug wholesalers to become two, arguing consumer prices would rise. Last year, the FTC also blocked Staples Inc. from acquiring Office Depot Inc.; it claimed the combination would limit competition in the office-supply superstore sector.

Regulators aren't just concerned with deals between competitors. They're also eyeing vertical hookups between suppliers and major customers. In the Lockheed-Northrop case, Justice worries about the implications of a marriage between a fighter-jet manufacturer and a maker of radar and electronic countermeasures in a vastly shrunken defense industry. If the merger goes through as proposed, Raytheon Co. and ITT Corp., Northrop's chief rivals in the electronics field, fear they would be left with only one plane customer—Boeing Co. So Justice wants full divestiture of Northrop's electronics business.

BEYOND MERGERS. Since getting the electronics was a key reason for the deal, Lockheed will fight hard to keep it but will counter with a less radical spin-off and other proposals to preserve competition. The plan "will address Justice's concerns," says spokesman Charles P. Manor.

Trustbusters are also looking beyond mergers to other allegations of anticompetitive practices. The FTC is now investigating whether MasterCard and Visa are forcing merchants who accept their credit cards to use their less popular debit cards as well, a practice that could dampen debit-card competition.

And in what would be the biggest antitrust action in decades, Justice is weighing a broadscale suit against Microsoft for compelling computer makers to take both its Internet browser and software.

If the new push for antitrust enforcement is giving Corporate America pause, it's hard to detect. Deals are proceeding at the same staggering pace, and with investors demanding an ever improving bottom line, companies still would rather take their chances with an aggressive Washington than face disappointed investors on Wall Street.

By Susan B. Garland, with Stan Crock and Catherine Yang in Washington, D.C., and bureau reports

WASHINGTON

PRIVATIZE SOCIAL SECURITY?

Soon, the question may not be whether, but how much

COMMENTARY

By Mike McNamee

YES: THE PRIVATE MARKET OFFERS BETTER RETURNS

Whom are you going to trust to watch over your retirement? The wizards of the federal government—or yourself? In the end, that question will dominate the Social Security debate. And ultimately, given the American preference for the individual over the state, the answer will likely involve privatizing.

Privatization can mean many things, from direct government ownership of stocks to wiping out Social Security. But the middle-ground fix that's likely to emerge will look like this: Workers would set up accounts funded by about 1.4% of the current 12.4% Social Security payroll tax. Another 1.5% in new payroll taxes from workers and employers would be added to the accounts. With this, workers could invest in stocks, bonds, and money markets.

STOCK ANSWER. Today's retirees and 55-plus workers would stay in the old system. The 11% of payroll still flowing into it would continue to fund a safety net of a slightly reduced basic pension, plus disability insurance and survivor benefits.

When today's twentysomethings retire, that basic benefit might pay only 75% of what Social Security promises now. But those workers would more than recoup the loss from the 45-year build-up in their private accounts, which were tapping into market advances. While there is no doubt a risk, equities have for seven decades delivered around 8% real annual gains, vs. Social Security's return of 1.5%. Under limited privatization, today's 25-year-old couple with average earnings would net 10% more retirement income than today's system promises.

Higher returns are often seen as privatization's main benefit. But the real reason Social Security needs private accounts is to build up savings in the system. Since 1939, Social Security has operated on a hand-to-mouth basis, using taxes from this year's workers to pay this year's benefits. That won't work when the baby boom retires: "It's hard to see how we can go from more than three workers supporting each retiree to two workers per retiree," says Deputy Treasury Secretary Lawrence H. Summers.

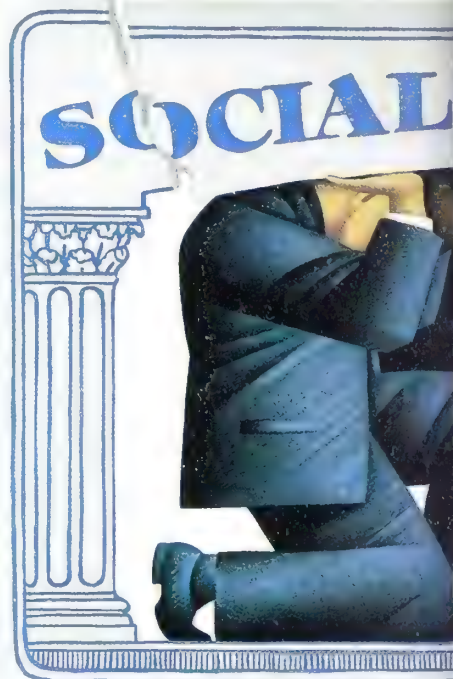
The 1983 reforms were aimed at squirreling away surpluses into a trust slated to reach \$3 trillion by 2019. But those overages weren't saved. Instead, the extra cash was siphoned off to cover government deficit spending. That shows that funding in advance of need can work only if the funds are safely out of politicians' reach. So Social Security, the only pension fund in the world that doesn't buy stocks, has to get into the market. And unless Americans want Washington to own a chunk of Corporate America, the only way left is private accounts.

Growth optimists say radical changes aren't needed because swelling payrolls will solve the problem. But even if productivity grows above the 1960s' boom pace for the next 75 years, Social Security actuaries estimate that as much as half of the Social Security shortfall will remain unfunded. Defenders of the government-run system point to stock-market risks. But for all but the lowest-paid workers who collect more

On Apr. 7 in Kansas City, President Clinton kicks off a series of town meetings to discuss the plight of the Social Security system, which some economists fear could be tapped out by 2030. Clinton, who called for Congress to allocate anticipated budget surpluses for a Social Security fix during his State of the Union address in February, has now found a surprising ally in House Speaker Newt Gingrich. On Mar. 5, the Speaker urged fellow Republicans to postpone income-tax cuts and make

than they put in by design, today's system returns less than Treasuries.

The focus on pitfalls ignores the biggest danger: inaction. According to Social Security trustees, even traditional fixes will cost workers and retirees the equivalent of an 18% tax



hike. Voters won't pay that tab if they get nothing in return. Private accounts—blended with a healthy public safety net—offer a tangible gain. Americans won't accept anything less.

McNamee follows Social Security reform from Washington.

Security salvation their crusade
lection year, too.
though there is no consensus yet
ow to solve the Social Security
—or whether a heroic rescue is ac-
needed—Democrats and Republi-
are both talking about some form
privatization. Indeed, the politics of
ssue are coming down to a debate
how much privatization is justi-
rather than whether any is appro-
at all. Wall Street interests, not
isingly, are pushing for the maxi-

mum, since privatization would bring a
new flood of money into mutual funds,
bonds, and other investments.

Under one compromise scenario, about
21% of one's annual Social Security tax
payment would be handed back to the
individual for investment in stocks and
bonds. Like a 401(k), the account would
be subject to the upticks and downturns
of the markets. But proponents argue
that given the long-term record of rising
equity markets, the potential for
impressive returns would more than

make up for the additional risk.

BUSINESS WEEK's Michael McNamee
and Christopher Farrell take up the op-
posing sides of the debate. McNamee
argues that a system of partial privati-
zation would be the best solution. Far-
rell says the transformation of Social
Security from a social safety net into a
more risky investment system would
violate the founding principles of the
program and unnecessarily risk the
monthly retirement checks that those
most in need depend on.

COMMENTARY

By Christopher Farrell

NO: WHY LET WALL STREET GAMBLE WITH OUR NEST EGG?

■ everybody knows Social Security is
■ a basket case, right? For years,
■ critics have warned that insolvenc-
looms without radical changes.
Recently, they have stepped up
their attack, painting it as a terrible
investment as well. Let people invest

the local Charles Schwab & Co. of-
fice, let's review the bidding. Yes, the
long-term inflation-adjusted return
on equities is around 8%, a figure
that dwarfs the 1.2% to 1.5% real re-
turns on Social Security.

Yet, it is an axiom of economics:

Higher returns always are at-
tached to investments that pose
greater risks. Equities are not
predestined to go higher and
sometimes, for years, they don't.
Thus, returns on Social Security
should be lower because it is es-
sentially a riskless security in a
taxpayer's portfolio.

Still, wouldn't workers do
better if they could invest in
government bonds, a safe har-
bor with long-term real returns
of 2.1%? Problem is, Social Se-
curity has promised trillions of
dollars to older workers and re-
tirees under the current sys-
tem. These obligations would
have to be met with increased
taxes during the transition to
the new system, and the higher
taxes would cut into the bond-
market rate of return.

The Social Security safety net
also offers features the private
sector has great difficulty match-
ing, such as portable insurance
that covers the variables of one's
earnings, length of life, disability,
and inflation. The system is remark-
ably efficient, with administrative costs
a razor-thin 0.8% of benefits paid. "So-
cial Security was not meant to be a
get-rich scheme or a competitor to go-
go funds," says Robert Eisner, econo-
mist at Northwestern University.

But don't we need Social Security

reform to boost national savings?
Hardly, since consuming less today
does not automatically mean more
economic growth tomorrow. The
U.S. economy has been a world-beat-
er over the past decade, with high
rates of investment in information
technologies, even though Americans
save much less than the Europeans
or Japanese. In a knowledge econ-
omy, money follows innovations. In
the end, as John Maynard Keynes
told us, economic growth depends on
the animal spirits of capitalism.

REPAIR KIT. Indeed, what really mat-
ters is not savings but strong produc-
tivity growth. The system's prospec-
tive tab will be much easier to meet if
rapid productivity growth fattens
worker wallets and increases the
overall tax take, as it did these past
two years when the rate approached
the healthy levels of the '50s and '60s.

Social Security still could use some
repair work. For instance, econo-
mists agree that developing a more
accurate measure of consumer prices
so that cost-of-living hikes don't ex-
ceed inflation would close part of the
system's long-range deficit. Another
change: extend Social Security to the
nearly 4 million state and local gov-
ernment employees, who, while not
eligible for coverage, are also not
paying FICA taxes.

Social Security has long struck a
delicate balance between individual
equity and social adequacy. It is a
compact between generations that
would be upset by privatization.

*Farrell, a baby boomer, believes
Social Security will be there when he
retires.*



me—perhaps even most—of their
x contributions in the capital mar-
ts, especially stocks, the naysayers
gue. Workers would earn a better
turn, and the economy would boom
on increased savings.

But before you get ready to take
our Social Security money down to

DETROIT

SLIP SLIDIN' AWAY AT GENERAL MOTORS

How low will its market share go? A dwindling lead over Ford

GRAND PRIX:
DIMMING STAR



Last June was a grim time at General Motors Corp. The company's share of U.S. light-vehicle sales skidded to a 71-year low of 28.4%. GM executives were quick to place the blame on short supplies caused by strikes at two key plants and the startup of manufacturing of nearly a dozen new models. GM brass promised that by fall, the shortages—and the decline—would end.

They did. But not for very long. By late 1997, GM's market share bounced back to finish the year at 31.1%—a far cry from the 49% the No. 1 auto maker once commanded, but enough to shore up GM's assertion that its three-decade slide in market share was over. Then came 1998. In January, sales dipped 6%, and in February 7%, leaving GM with a miserable 28.6% share. "It looks disastrous to me," declares Martin J. "Hoot" McInerney, a suburban Detroit Cadillac dealer. "When is GM going to realize the trouble it's in?"

This time, GM has run out of excuses. The heralded new models have long since arrived in sufficient numbers, along with expanded production of lucrative large sport-utility vehicles. Across the U.S. market, demand remains solid, and GM is enjoying a rare period of labor peace. Given that, some analysts figure its share will hover between 27% and 29% unless the company pours on the rebates. "I'm not optimistic about their share coming back without a lot of money being spent," says Furman Selz Inc. analyst Maryann N. Keller.

That leaves GM in a tough position. It's in danger of losing the lead to archrival Ford Motor Co. for the first

time since 1931. And its 8,090 dealers, especially at such shaky divisions as Oldsmobile, badly need hot-selling cars to stick with GM. Worse, profits quickly evaporate when factories run below full capacity because of fixed overhead costs, including labor. The company's share has been dwindling faster than it can close plants, and the constant downsizing only exacerbates already rocky relations with unions.

FAT PROFITS. GM execs, who earlier this year predicted modest share gains, won't talk now. But in a press release, marketing chief Ronald L. Zarrella said that while sales of midsize cars and minivans were "very encouraging—there is no denying this is going to be a very tough, very competitive year for us." Earlier, he told BUSINESS WEEK that the company is shrinking its operations to make itself profitable at 32% to 34% market share. He admits that if GM misses that share target, it may again have to cut capacity. Already, GM has trimmed first-half production by 2.5% from last year's levels, to 2.18 million vehicles. And G. Richard Wagoner Jr., GM's president of North American operations, has hinted that GM would eventually close the Ste. Therese (Que.) plant that builds Pontiac Firebirds and Chevy Camaros if it can't make those cars profitably.

So far, investors aren't alarmed. Delighted with GM's record profits last year and enamored of its current \$4 billion stock buyback, Wall Street has recently been pushing GM shares to all-time highs of \$74.25. However, says Lehman Brothers Inc. analyst Joseph Phillippi: "If you look at the trees instead of the forest, this stock should probably be about 60."

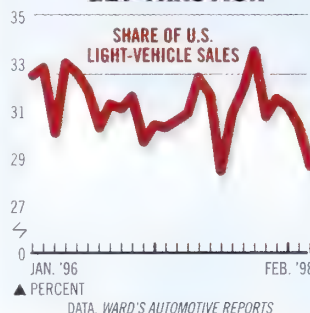
So what happened to GM's comeback? For starters, the company is overly concentrated in the shrinking small-car market, where sales of its five subcompacts have tumbled 30%. Yet even in the red-hot large sport-utility segment, the Chevy Suburban is down 11% and the GMC Yukon has dropped 13%.

True, as GM's press release boasts, its five new midsize sedans—including the Chevy Malibu and Buick Century—are well above year-ago levels, but that's when these models were in short supply. Compared with the more typical February, 1996, these new models undersold the old GM midsize cars by a scary 31%. And the redesigned Pontiac Grand Prix, the first solid hit among the

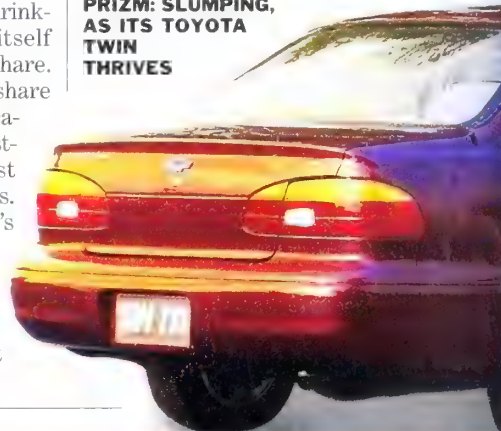
new cars when it was launched in summer, 1996, slipped 23% in January and February.

The sad conclusion: GM's new models are disappointments. "Not one is selling close to where it's supposed to be," says Wes Brown, an auto consultant at NexTrend Inc. For instance, since the beginning of the year, monthly sales of the three new minivans have been just under 12,500—a pace that will fall about 50,000 short of GM's 200,000-a-year-goal, he notes. Likewise, Malibu, selling about 15,500 monthly,

GM JUST CAN'T GET TRACTION



PRIZM: SLUMPING,
AS ITS TOYOTA
TWIN
THRIVES



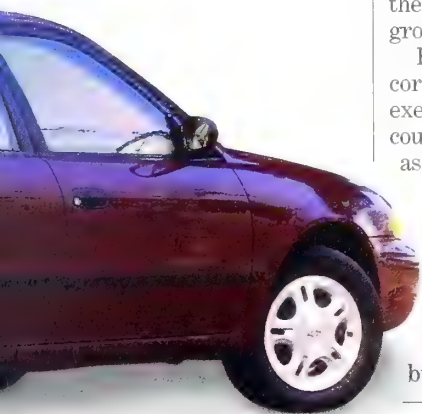
short of GM's 16,000 to 18,000-unit volume. "GM has a lot of new hardware and a lot of old brands," says Schroder analyst John Casesa. "It's going to take years of new products and new marketing and promotional spending to establish these brands."

The sign of how tarnished GM's image has become: Chevy's sales of subcompacts fell 30% in February, while sales of near-identical Toyota Corollas built by a GM-Toyota Motor Corp. venture in California, rose 4%. Options for a fast U-turn are unclear: Bigger rebates, subsidized leasing, or low-rate financing squeeze profit. Discounting in general runs counter to GM's vaunted brand-management strategy of tailoring a distinct identity to each model and commanding full price. He says cut-rate deals undermine GM's image. And GM has sworn not to go to another quick fix that backfired in the early '90s—massive but low-rental-fleet sales.

EMERGENCY MEETING. On Mar. 4, it put together rebates on its three new mini-cars. Dealers are getting \$750 cash rebate to sell Suburban and Yukon SUVs. On Mar. 1 announced it would subsidize a \$299-a-month lease on the slow-selling Grand Prix. And the company on Mar. 10 kicked off its spring promotion offering 1.9% financing on most models. At Chevrolet, where February sales plunged 19%, sales managers called an emergency Saturday meeting on Mar. 7 to weigh possible remedies.

A year ahead won't get any easier. GM faces formidable launches of high-end vehicles: the new Pontiac Grand Prix and Olds Alero compact cars this year, and full-size pickup trucks this year. GM admits these startups could temporarily cut output and hurt sales. The good news is that analysts expect the pickups and the Grand Am to be strong sellers. However, if GM can't turn up sales of the rest of its lineup, it will eventually look back fondly at June, June and February, 1998—as the good days when market share topped 28%.

By Kathleen Kerwin in Detroit



WASTE TRUCK IN OAKLAND, CALIF.: A STUNNING FALL

DEALS

CAN WASTE MANAGEMENT CLIMB OUT OF THE MUCK?

It's betting a merger with USA Waste can fix a heap of problems

Where most people looked at piles of refuse and saw plain old garbage, Wayne Huizenga smelled fame and fortune. Thirty years ago, they began cobbling together some 3,000 mostly family-owned waste-hauling businesses to forge the national network of garbage hauling and hazardous-waste operations known as Waste Management Inc.

Today's Waste is still the largest player in the garbage industry. But otherwise, it is hardly recognizable. Huizenga left in 1984. Buntrock, Waste's long-time chairman, who had retired only to be rushed back into service in 1997 when his successor, Phillip B. Rooney, resigned under investor pressure, was nudged off the board at the end of that year by a group of outside directors.

Humbled by severe downturns in its core markets, poorly timed and badly executed expansions, and self-inflicted accounting gaffes, once-proud Waste's fate as an independent company was sealed on Mar. 11. In a stunning acknowledgement of its fall, Waste agreed to be acquired in a \$13.5 billion transaction by USA Waste Services Inc., a company with less than one-third its \$9 billion in sales. Waste, the creator of the modern garbage business, is turning itself over to a

management team led by USA's acquisition-minded chairman, John E. Drury, an industry veteran who just joined USA four years ago.

It was the best news Waste's shareholders had seen in years. Its share rose 16.4%, to 29%. Investors such as Nell Minow, a principal at Lens Fund, were particularly pleased. Recently, Minow has been agitating for Waste to do a deal. Equally happy is another long disgruntled holder, Soros Fund Management, owner of 6.2% of Waste. Says Soros Managing Director Stanley F. Druckenmiller of Drury: "This is the best CEO in the industry." Druckenmiller and Minow are convinced that Drury will be able to quickly wring at least \$800 million in costs out of the combined company.

INCONSISTENCIES. The deal might have been done months ago. Drury approached Robert S. "Steve" Miller, an outside director and turnaround specialist when he was appointed interim chairman and CEO on Oct. 29. Miller thought the company could survive on its own. But that was before he started digging into its problems—and before his Feb. 24 bombshell. That day, Miller announced \$3.5 billion in charges to clean up the company's books—restating five years of earnings and taking massive charges to adjust for overambitious accounting practi-

ces. The charges covered everything from overvalued acquisitions to questionable treatment of landfill assets—a “sobering and embarrassing” series of missteps, says Miller, adding: “This merger makes it much easier to change the operating dynamic at Waste.”

The write-offs illustrate how important such change will be. Behind those numbers, according to interviews with more than a dozen former senior officials who refused to be quoted by name, lie accounting procedures riddled with inconsistencies. District officers were allowed to set their own pricing and determine the useful life of landfills for accounting purposes. For example, one former district controller in the Southwest says he never assigned scrap values on trucks and containers, while one in the Southeast says he always looked for the best deal. There could be different definitions of a “route hour”—how the company allocated costs to a driver’s work—that could affect how a district priced contracts. “There was no consistent operating model,” says a former headquarters exec. “It was dysfunctional.”

SO MANY DUMPS. Waste’s growth even more flaky when aggressive accountants consolidated results back in the Oak Brook (Ill.) headquarters. Miller and former officials say the bean counters used depreciation schedules and asset valuations that were even more optimistic than those set in the field. In district offices, for instance, trucks and containers were depreciated according to industry standards—8 years on trucks, 10 on containers. But at headquarters, equipment was depreciated over as many as 13 years, enabling the company to minimize annual expenses. The total hit to adjust for depreciation for trucks and equipment: \$716 million.

There were major lapses, too, in accounting for landfill development, write-offs for areas that were never granted permits, and environmental liabilities. Former officials say areas where permits were denied would be kept as assets a bit longer than they should have been, one former con-



“SOBERING AND EMBARRASSING”: Accounting problems led CEO Miller to take \$3.5 billion in charges

troller says. If permits were being sought for a given amount of space for a landfill, with plans for more later, the larger asset might be booked, says another former official. The cost just to fix improper accounting for capitalizing the interest expense on landfills: \$210 million.

The breakdown in accounting procedures appears to have happened as the company’s growth screeched to a halt in the early ’90s, as the basic business softened and its diversifications faltered. Waste was saddled with a surplus of dump space and faced declining prices. As its stock stalled, acquisitions were no longer feasible, thereby cutting into growth. One way out was a costly overseas push. Another, it now appears, was

to try to mask the problems with accounting. Says Miller: “The best we can guess is we got off track in the ’90s, coincident with our declining fortunes.”

But Waste’s problems went beyond accounting. As revenue growth stalled, the company lurched from strategy to strategy—one year urging regional operatives to boost market share the next to focus on profitable accounts. Former execs say that led to confusion and declining morale. “We would benchmark against GE or FedEx, but because it might take years to put in place, we didn’t have the fortitude to stick with it,” says one **FINGER POINTING.** Who is responsible for Waste’s woes? Investors and analysts blame a cast of characters—Buntrock, Rooney, former Chief Financial Officer James E. Koenig, and Waste’s long-standing auditors, Arthur Andersen & Co. Miller has pledged to get to the bottom of who “should be held responsible

among our executives and auditors,” but is not pointing fingers yet. Lens’s Minow has no qualms: “Andersen owes the shareholders some money. They are there to prevent exactly this kind of surprise, and we urged them to switch auditors.” Rooney, Koenig, and Buntrock declined comment on who was responsible. Citing firm policy, Andersen declined to discuss Waste.

Drury vows to get the new Waste back on track—and back on the acquisition trail. “We see this becoming a much bigger business,” he says. “We can grow the top line 11% to 15% on its much larger base.” That’s fine—as long as he manages accounting better than the old Waste did. Melissa M. White an analyst

at Piper Jaffray Inc. and a former Waste official, notes that USA, like Waste in its early days, has been run leanly and in a decentralized fashion. “One of the biggest risks is whether they have the right systems and controls in place” for a much bigger company. If not, can this combo stay at the top of the heap?

By Richard A. Melcher in Chicago, with Gary McWilliams in Houston

THE MESS AT WASTE MANAGEMENT

WMX restated earnings for 1992-97 and took write-downs. Cost: \$3.5 billion

OVERVALUED ASSETS...

	MILLIONS
Overvalued landfills, other waste sites and facilities	\$1,300
Depreciated equipment and trucks too slowly	754
Overstated goodwill	536
Overstated value of investments in other companies	109
Other	185

...AND UNDERVALUED LIABILITIES

Reserve for environmental liabilities too low	\$287
Losses on contracts understated	137
Insurance reserves kept too low	83
Severance costs underestimated	60
Other	87

DATA: WASTE MANAGEMENT INC., BUSINESS WEEK

FLIES

IE BANE OF BUSINESS BACK

er & Me's Michael Moore takes on corporate greed



With its sleek marble lobby, modern art, and security guards, the tower on Manhattan's Upper West looks like the kind of building from which *Roger & Me* filmmaker Michael Moore usually gets ejected. But the pro-union provocateur from Flint, Mich., who made so much money from movies, television, and a book that he's now on the outside looking in. He's here. That newfound wealth lends ironic subtext to his latest movie, a documentary about corporate greed called *The Big One* to be released on Apr. 3.

Not that Moore has gone soft. Quite the contrary, he has gone from mock-er of former General Motors Corp. chairman Roger B. Smith in *Roger & Me* to lambasting all of Corporate America. Still dressing and talking like a scruffy auto worker with attitude, Moore hopscoches the country slandering Pillsbury for accepting "corporate bribes," Borders bookstore chain for

fighting unionization, Johnson Controls for moving jobs from Milwaukee to Mexico, Trans World Airlines for using convicts as telephone reservation agents, and Procter & Gamble for cutting thousands of jobs while racking up record profits. Moore goes one-on-one with Nike Inc.'s Philip H. Knight about using teenage girls in Indonesia to make sneakers. "One evil empire down. One to go," he says near the end of the film. **NOBLE SARDINE?** But it's not capitalism that Moore seeks to extinguish, just the unbridled greed that often accompanies it. In fact, Moore even embraces the perks of the corporate class. In one scene, he unapologetically uses a first-class plane ticket, paid for by his *très* corporate publisher Random House Inc. during the speaking tour for his 1996 book, *Downsize This! Random Threats from an Unarmed American*. "There's nothing noble about sitting like a sardine back in row 37 in the middle seat," Moore says now. In another scene, he

discovers that Random House's promotional campaign has catapulted his book to *The New York Times* best-seller list and exults, only half ironically: "Now, I don't think corporations are such a bad idea!"

But Moore insists that he can fly first class without forgetting what it's like to ride on Greyhound. He claims that his old friends from Flint never tease him about his windfall: "They're all happy that one of us got out. One of the basic tenets of the working class is you want to get out of the working class," Moore says.

A TIGHT LEASH. Remembering his roots, Moore has given \$500,000 in grants to charities in Flint and to other independent filmmakers. Where Moore parts company with many of his fellow first-class passengers is in his conviction that capitalism needs a tight moral leash.

One particularly tense scene in the mostly lighthearted movie comes when Moore confronts executives from Johnson Controls Inc., which is shifting manufacturing to Mexico. Moore tries to present Johnson's chief executive officer with an

ANTISTYLE
Despite his considerable success, Moore still dresses and talks like a schlubby auto worker with attitude

oversize check for \$80¢—the amount, he says, that the company will pay for an hour of Mexican labor. Tight-lipped company executives give Moore the bum's rush as he hands over one of his "Downsizer of the Year" awards.

The Big One borrows gags from *Downsize This!* and his two-season TV series, *TV Nation*. In a typical riff, Moore suggests renaming the U.S. "The Big One," changing the national symbol from the bald eagle to the bald man, and switching the national anthem to that sports-arena classic, *We Will Rock You*. Another time, he postulates that the unblinking Steve Forbes comes from another planet.

Moore is more of populist wise guy than a leftist theoretician. In fact, he avoids giving specific policy prescriptions. "I'm a person with a high school education. I'm not going to come up with the ultimate solution to these problems," he says.

Moore says that he made *The Big One* to comfort those who have been left behind by the New Economy—"so for 1½ hours, they'll feel some cathartic sense of, 'Here's one for our side.'" Evil empire rhetoric notwithstanding, Moore turns out to be about as Marxist as Groucho.

By Peter Coy in New York

EDITED BY KELLEY HOLLAND

PG&E'S BIGGEST POWER PLAY YET

DEREGULATION MAY BE A threat on the home front, but PG&E figures that it can be a business opportunity out of state. The San Francisco parent of Pacific Gas & Electric, which is pushing to sell its services outside California in order to counter impending electricity deregulation there, is also signing agreements to sell its expertise throughout the U.S. Its biggest coup so far came on Mar. 10, when PG&E signed a \$2 billion deal to provide power to Ultramar Diamond Shamrock's seven refineries, its pipelines, and its network of 2,400 combination gas station-convenience stores. In addition, PG&E will

build a 750-megawatt cogeneration plant to provide steam and electricity for Ultramar's Three Rivers (Tex.) refinery.

HOW MUTUAL FUNDS CAN SAVE TREES

QUICK READ: THE SECURITIES & Exchange Commission ruled on Mar. 10 that mutual-fund companies are allowed to sell their wares using a three- to six-page document called a profile instead of a lengthy fund prospectus. The commission also revised its disclosure requirements for prospectuses, which investors will still receive after they invest in funds, omitting such information as descriptions of a fund's capital structure. "It's time investors had useful information before making a decision instead of incomprehensible, dense documents," says Kathleen Clarke, the commission's assistant director of the division of investment management.

SATURN'S CONTRACT STAYS IN ORBIT

IT'S STILL A DIFFERENT KIND of car company. Union workers at General Motors' Saturn division on Mar. 11 voted to keep their innovative contract, often deemed a model of union-management cooperation. Saturn's members called the vote because Saturn sales are down 20%, which they feared threatened their bonuses and job security. After the vote, union chairman Michael Bennett blasted GM for failing to commit new capital and products to Saturn: "The partnership is alive and well at Saturn," he says. "But GM has yet to live up to its part of the bargain." He warned workers won't continue their unusual alliance forever without greater support from GM.

HEADLINER: LEE KORINS

DECLARATION OF INDEPENDENCE IN PHILLY

Leopold Korins' personal stock took a hit Mar. 9, when the Philadelphia Stock Exchange announced its chairman and CEO as resigning because of a difference with the board over strategy. Korins, a 32-year Merrill Lynch veteran who ran the Pacific Stock Exchange from 1990 to 1996, took over the struggling Philly bourse last August.

Korins, 64, arrived in Philadelphia at a difficult time. In 1996, then Chairman Vincent Casella resigned after it was revealed he had a financial interest in a company that had been selected to install a new trading system. Under pressure

from the Securities & Exchange Commission, the exchange then adopted a sweeping governance overhaul.

Reforms included a more independent board of directors, and sources close to the exchange say the board was frustrated with Korins' progress in addressing regulatory problems.

Korins couldn't be reached. There is talk that Korins' exit could lead to a merger with another bourse—maybe the Chicago Board Options Exchange. A Philly bourse board member says his exchange prefers to remain independent but would consider any proposals.

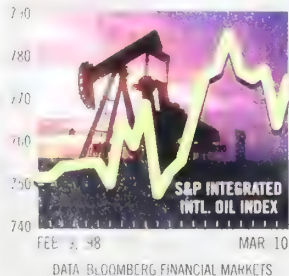
By Amy Barrett



CLOSING BELL

MINI-GUSHER

With the world awash in crude, major international oil companies have underperformed the market all year. After a strong performance since Feb. 23, they took a hit on Mar. 9 after Saudi Arabia vowed not to cut production: The S&P index of integrated global oils dropped 1.6%, to 764. But it's bouncing back. On Mar. 10, PaineWebber oil analyst Frank Knuettel, a onetime bear, upgraded the sector, saying the worst may be over. That spiked the index up to 775.



A NEW PLAYER IN SET-TOP BOXES

MICROSOFT ISN'T THE ONLY computer giant in cable set-top boxes. On Mar. 10, Network Computer, a joint venture of Oracle, Netscape, and others announced a deal to supply software and set-top boxes to Cable & Wireless for use in up to 7 million homes and businesses in the United Kingdom, Australia, and Hong Kong. Installation is expected to start this year in the U.K.—far ahead of TCI's rollout, according to NCI CEO David Roux. "This gives NCI credibility," says Cynthia Brumfield, an analyst with Paul Kagan Associates, a cable market research firm.

DILLER'S TICKET TO MORE RICHES?

BARRY DILLER'S FLEDGLING media empire continues to expand. On Mar. 10, his USA

Networks struck a \$386 million deal to buy half of ticketing agency Ticketmaster Group USA, which operates the Home Shopping Network and the recently acquired USA and Sci-Fi Networks, is expected to use Ticketmaster as part of its plan to create a TV network based in part on infomercial-style programs that sell products directly to viewers. Ticketmaster CEO Fred Rosen will leave the venture.

ET CETERA...

- Not smokin': Consolidated Cigar forecast disappointing earnings.
- Xerox will sell its Crum & Forster unit to Fairfax Financial for \$680 million.
- UBS and SBC said combined 1997 earnings rose 60% from money management.
- Tobacco companies are seeking a mistrial in Minnesota's suit against them.

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BY OWEN ULLMANN

THE TOBACCO DEAL: SUDDENLY, THE CORPSE IS STIRRING

ball hung over the National Governors' Assn. winter meeting in late February—and with good reason. The guys thought they had come to pronounce last rites over \$365 billion national tobacco settlement and say goodbye to the fat cuts their states would get from the deal. Indeed, Hill Republicans and Dems bitterly divided, Iowa Gov. Terry E. Branstad declared the 1997 accord between attorneys general and Big Tobacco “dead.”

Well, somebody better call the undertaker, because the deal has sprung back to life. Fearing a backlash if they let the measure die, President Clinton and key members of Congress are laboring to collar the votes for agreement this year. Their goal: to ensure states and the feds get their hands on the megabucks a tobacco deal would generate.

Signs of compromise are cropping up all over Capitol Hill. Such makers as Senate Commerce Committee Chairman John McCain (Ariz.), House Commerce Committee Chairman and longtime industry defender Tom Bliley (R-Va.) and anti-tobacco Representative Henry Waxman (Calif.) all say they're open to a bipartisan solution. “We’re seeing a weird phenomenon taking place,” notes a veteran White House staffer. “People are actually trying to be statesmen.”

NOTHING. Clinton, needled by GOP leaders for failing to spend enough political capital on a deal, has launched an offensive of his own: He's calling for a massive industry-funded campaign to curb teen smoking as part of any agreement. Republicans, for their part, want to avoid the “do-nothing” come the fall elections. At the same time, the GOP covets tobacco cash to pay for tax cuts and new health programs.

By persuading the industry to sign off on a tough, bipartisan bill, Republicans hope to deflect Democratic charges

that they're captives of a special interest that has funneled millions into GOP campaign coffers.

Other hopeful signs: Big Tobacco, launched an ad campaign on Mar. 11, calling for congressional action. The next day, a bipartisan group led by Senator John Chafee (R-R.I.) planned to unveil a compromise that would finance the deal with a \$1.50-per-pack hike for cigarettes over two years.

The improved odds for an accord can be seen in the shifting public pronouncements. A month ago, GOP leaders were blasting Clinton for proposing new social initiatives financed with illu-

sory tobacco-deal dough. Now, House Speaker Newt Gingrich (R-Ga.) and Senate Majority Leader Trent Lott (R-Miss.) talk of using the money for tax relief or entitlement reform. “There is [now] an assumption that Congress is going to pass comprehensive tobacco legislation,” says White House domestic policy aide Elena Kagan.

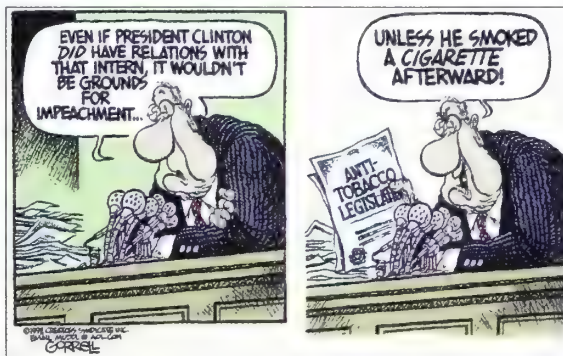
Getting a deal remains tricky, given all the feuding Hill barons with overlapping jurisdictions. After a let's-reason-together session

called by McCain on Mar. 11, the senator said there was “some agreement [on] broad parameters.”

But even if the turf wars can be halted, Clinton and Congress must solve two potential dealbreakers: how much protection to give Big Tobacco from legal action, and whether to pay billions in fees to trial lawyers who represent the states. Some public-health groups have vowed to kill a deal they find too industry-friendly; trial lawyers have sworn the same fate for a pact they judge to be attorney-hostile.

Nobody minimizes the obstacles ahead. Cautions McCain: The coalition backing the agreement is “very, very fragile.” Still, the tobacco deal doesn't look ready for burial just yet.

By Richard S. Dunham



CAPITAL WRAPUP

TT'S LOOSE LIPS

Senate Majority Leader Trent Lott (Miss.) may pay a bigger political price than House Speaker Newt Gingrich (R-Ga.) for shooting from the hip. Lott was forced to back down after he suggested on Mar. 6 that independent Counsel Kenneth W. Starr should quickly wind up his probe of President Clinton. Three days later, amid a firestorm of Republican criticism, Lott reversed himself and said Clinton should stop onewalling.”

Gingrich, meanwhile, was criticized by GOP tax-cutters for agreeing with Clinton that any budget surplus should be used to stabilize Social Security. He now says he's for big tax breaks and entitlement fixes.

Republican insiders tend to give Gingrich a break: They say he often makes provocative statements to stimulate debate. But GOP activists say Lott is eroding confidence in his leadership by frequent impolitic pronouncements. Even Gingrich says he doesn't understand what his pal Trent was thinking.

SPENDING THE SURPLUS

► How will Congress spend the growing budget surplus? The first chunk of extra change could actually go to the Pentagon. The military may get \$2 billion to cover U. S. troop deployment in the Persian Gulf and the continued cost of keeping troops in Bosnia. In the past, unexpected overseas missions came out of procurement. But Congress seems likely to agree to use strong tax receipts to cover the tab for keeping Saddam Hussein in check and Bosnia quiet.

THE CRISIS AT SAMSUNG

Will the giant make needed changes?

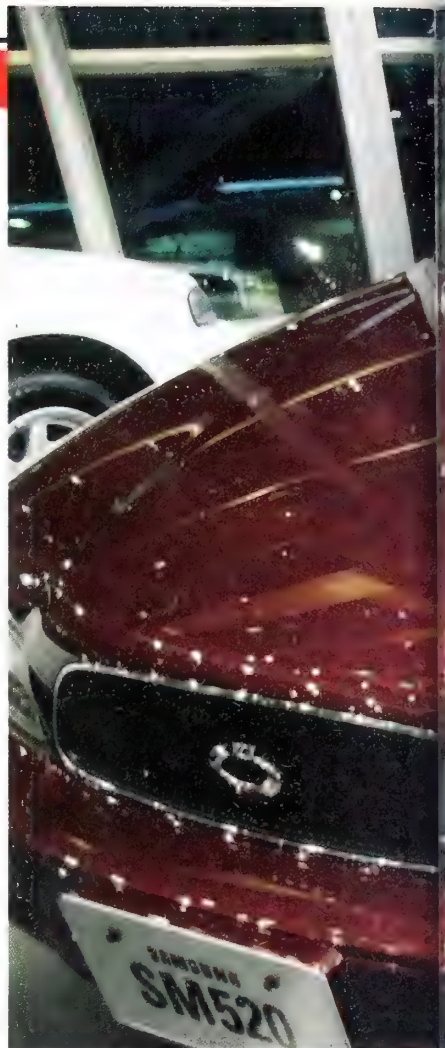
Samsung Group Chairman Lee Kun Hee defies easy characterization. As South Korean *chaebol* chairmen go, he's as autocratic as any. Yet last November, he authored a book, *Look Around the World and Think*, that urges Koreans to shape their own destinies during times of upheaval. He spends weeks at his palatial home mapping out his grand strategies. Then suddenly he's obsessing about details, browbeating managers over squeaky washing machines, or test-driving a prototype of Samsung's new SM5 sedan.

The chairman—no one at Samsung ever calls him Mr. Lee—has used these tactics to reach a level of influence that no U.S. chief executive could ever match. Koreans shop at Samsung department stores, operate Samsung PCs, stroll through Samsung art galleries, chat on Samsung mobile phones, have operations at Samsung hospitals, and live in houses built by Samsung construction equipment. Many of the companies selling these products and services barely break even, yet Lee has added steadily to this sprawl, thanks to abundant loans from foreign and local banks that have regarded Samsung as the bluest of Korean blue chips. And

inside the group, Samsung Electronics, the world's dominant memory chip maker, has bankrolled other Samsung businesses, even guaranteeing \$4.5 billion of their debt.

Yet not even a dynamo like Lee can reverse the effects of the Asian crisis and a slump in the global chip business. Both events have conspired to deprive Samsung of what it needs most—ready cash to prop up profitless companies, service billions in debt, and embark on imperial adventures like the new auto business. As a result, Lee faces a choice—change Samsung radically, or risk fatally weakening his group, especially the core chipmaking business. How he and his lieutenants tackle this task could well set the tone for all of Korea Inc.'s restructuring.

"TOUGH LESSON." Lee would not speak with *BUSINESS WEEK*, but five of his senior executives did. What emerges from these interviews is a willingness to change that no one thought possible just a year ago. Still, no bold plan has emerged to reinvent Samsung. That, say analysts, would involve laying off 20% of the workforce of 230,000, and selling off autos, petrochemicals, aerospace, and other laggards to focus on



memory chips, liquid-crystal displays (LCDs), telecom equipment, and financial services.

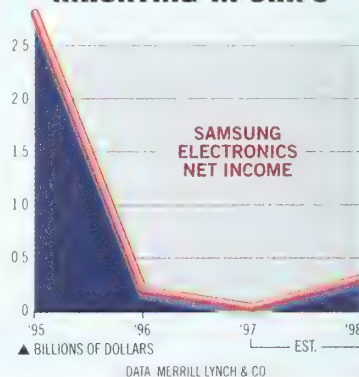
For now, executives are still adjusting to the idea that the heady days of breakneck expansion are over. "We are realizing that financial resources are very scarce," says Hwang Young Key, senior managing director and a member of Lee's powerful executive staff. "This is a very tough lesson for us." Group earnings, which plummeted 80%, to \$67 million on sales of \$93 billion in 1996, may even fall into a loss when Samsung re-

SAMSUNG IS AN EMPIRE...

COMPANY	SALES BILLIONS	PERCENT OF TOTAL	BUSINESS
SAMSUNG CORPORATION	\$29	32%	Trade, retail, apparel, other
SAMSUNG ELECTRONICS	19	20	Memory chips, PCs, phones
SAMSUNG LIFE	17	19	Life insurance
SAMSUNG FIRE & MARINE	4	4	Commercial insurance
SAMSUNG DISPLAY DEVICES	4	4	Liquid-crystal displays
SAMSUNG HEAVY INDUSTRIES	4	4	Ships, construction equipment
OTHER	16	17	Chemicals, aerospace, other

DATA: BUSINESS WEEK, COMPANY REPORTS, MERRILL LYNCH & CO.

...HURTING IN CHIPS





as the in-house cash machine. When chips reaped windfall profits back in 1994 and 1995, insiders say, profits flowed into questionable projects. The biggest potential blunder was the creation of Samsung's auto division, which got 21% of its paid-in capital from Samsung Electronics. After spending \$1.8 billion over four years, Samsung Motors Inc. is rolling out its first car, an \$8,500 sedan based on the Nissan Maxima—just when the bottom has fallen out of the Korean car market.

The grim outlook probably drove Samsung executives last fall to sound out Ford Motor Co. about an alliance. The speculation is that Ford might take as much as a 50% stake in Samsung Motors but would insist on taking the helm. But no outside auto company has ever succeeded in calling the shots in a joint venture with a Korean company.

Nor has any *chaebol* ever succeeded in achieving a dramatic restructuring. Lee certainly grasps the magnitude of the problems. The burning question is whether he's able to abandon the

old ways of doing business. When Lee was a student at Tokyo's prestigious Waseda University in the mid-'60s, he became enamored with Japan's *keiretsu*, close-knit webs of companies cemented by equity ties, investments, and other business relationships. Lee now wants to change his corporate culture—for several years he has been exhorting his troops to "change everything but your wife and children." But most of the top-down management practices remain.

Should Lee manage to remake Samsung, he can make his mark as the chairman that took this proud company to the next step and led the way in reforming Korea's economy. But to do that, Lee will have to repudiate decades of corporate practice—and doubtless reinvent a part of himself as well.

By Moon Ihwan
and Brian Bremner in Seoul

s its 1997 results in late March. The major problem is debt—oceans of it, \$23.4 billion owed to domestic and overseas banks. That's 267% of equity, and it's getting hugely expensive to service now that local interest rates have skyrocketed and banks are struggling at making more loans. Executives are now obsessing about ways to cut debt to about 150% of equity. In 1995, it was valued at some \$600 million, Sweden's Volvo has agreed to buy the construction-equipment business, and U.S.-based Clark Material Handling Co. will buy its forklift division. Samsung is cutting global investments by 30%, selling \$300 million in real estate and other assets, and shelving projects such as a planned 102-story skyscraper in Seoul. Petrochemicals may go.

WIND. Meanwhile, to inspire the troops, senior managers have taken a pay cut. Lee is donating \$70 million of his \$2 billion fortune and most of his \$6 million salary to company coffers. At headquarters, the thermostat is set so low that execs wear thermal underwear.

The big problem is that the keystone of Lee's empire—Samsung Electronics—now sits in a dangerously exposed posi-

tion. When the price of 16-megabit chips collapsed in 1996, it dragged down the unit's profits 93%, to \$194 million, vs. \$2.8 billion in 1995. Last year probably wasn't much better. Lee wants to diversify into higher-margin microprocessors, application-specific chips, and other logic chips used in everything from dishwashers to car-navigation systems.

Such a move up the food chain requires scads of cash. But Samsung Electronics is already laboring under \$6 billion in dollar-denominated debt, which is much harder to pay off with depreciated won. "Samsung Electronics is still king," says Daewoo Securities Co. analyst Jeon Byeong Seo. "But it's a king without much money." Small wonder that Samsung has started talks with Intel Corp. about a cash infusion. Both sides are keeping mum. But the betting is that Intel will pony up \$500 million for equity in Samsung, thus ensuring a steady supply of high-end memory chips when demand for its Pentium II microprocessor spikes at yearend.

Samsung Electronics probably would not be in such a fix if it had not served

ALL DRESSED UP

Samsung Motors is rolling out its first car, just when the bottom has fallen out of the Korean auto market

COMMENTARY

By Michael Shari

FOR SUHARTO, A MOST DANGEROUS GAME

The rumblings from Jakarta are getting ominous. For months, President Suharto has glibly agreed to reform his economy according to the stern dictates of the International Monetary Fund—then proceeded to stall on any moves that would weaken his grip on the economy. But in recent days, Suharto's lieutenants have fired up the rhetoric. Now, they say, their beleaguered leader may flat-out refuse to abide by the IMF's draconian edicts—and forgo its \$43 billion bailout package. Says Din Syamsudin, a top government adviser: "I'm afraid there's a communications breakdown between us and the IMF. Our people will say, 'Go to Hell with your aid.'"

Why would Suharto risk triggering a new Asian crisis and ruining his country's economy? It's possible the Indonesian President may be threatening to walk away from a deal to force the IMF to moderate its terms. Indeed, IMF Deputy Director Stanley Fischer on Mar. 10 did say the IMF would be "flexible" with the Indonesians. But the IMF, despite the nice talk, is refusing to cut any more checks until Suharto implements at least a few reforms.

ON THE BRINK. This game of brinkmanship is getting dangerous. Suharto would certainly like the IMF to cave and hand over the aid without any preconditions. But the nationalist rhetoric indicates Indonesia is contemplating some pretty scary measures to try to swim without the IMF's lifeboat. They include shutting Indonesia's economy off from the rest of the region and creating an Islamic banking system with no interest charges. "Indonesia would enter a shell, breaking ties with the rest of the world and moving into a closed economy status," says Rajeev Malik, senior economist at Jardine Fleming in Singapore.

In this scenario, Suharto may try a

variation on his currency board idea, fixing the rupiah to an exchange rate of 5,000 to the dollar—roughly twice its current value. To make that rate stick, Suharto would have to impose capital controls. That in turn would create a thriving black market in greenbacks and put the rupiah on a par with the inconvertible Burmese kyat or the old Soviet ruble. To get credit flowing inside the economy, Parliament Member Fadel Muham-



mad says Suharto would allow the injection of fresh capital into two small Islamic banks and maybe allow the creation of a third Islamic bank.

Suharto could also use his extraordinary powers to renege on regional free-trade agreements and start dumping Indonesia's abundant reserves of oil, timber, and precious metals on world markets to barter for food or earn hard currency. Of course, the country would have to default on its \$140 million foreign debt, now that usable foreign currency reserves have fallen below \$10 billion. A formal default would scare off international lenders for years to come.

The result could be the ultimate collapse of Indonesia's economy, which would cause regional instability as people riot and thousands of refugees stream out of the country into neighboring states such as Sin-

gapore. Vast recurring forest fires and a severe drought have also wrecked the rice harvest this year, making Indonesia no longer self-sufficient in food. The nation now imports its two most important staples, rice and flour for noodles. If things got too bad, the loyalty of the middle class and the army could wear thin enough to ignite civil unrest and a possible coup. Already, demonstrations are spreading. "It won't take

long for my staff to join in," says one bank executive. "The middle class is angry enough at Suharto to put a hatchet through his head."

Beyond fears of refugees and defaults is what Henry Kissinger termed the modern "domino effect." He's not talking about the old threat of communist hegemony but the possibility that countries such as Indonesia could fall away from the U.S. fold of free-market capitalism and open trade. That would cost the IMF plenty in credibility and perhaps lead South Korea and Thailand to renegotiate their own bailout packages.

Suharto's maverick maneuvering may force Washington and its Asian allies to rein in the IMF. He knows that if the financial crisis turns into a security crisis, his old allies in the State Dept. and the Pentagon could prevail over the U.S. Treasury Dept. and the IMF. The Asians are getting alarmed, too. In recent days, Singapore and Japan have explored the idea of extending their own aid to Indonesia to prevent a regional cataclysm. It's Suharto vs. the world. And the world fears the old man may not be bluffing.

Shari is BUSINESS WEEK's Singapore bureau manager.

WHAT IF...

Suharto may think he has nothing to lose by shunning the IMF, but the move would devastate his country

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COOKING UP JOBS

Spain's TelePizza increased its payroll by 62% annually from 1991-96. Its stock has soared from 14 to 123 since the '96 IPO

500 association, a non-profit group linked to the European Foundation of Entrepreneurship Research, identified 500 small and midsize companies whose sales—and employment ranks—are soaring. Conducted by IP Strategies, an independent consultant, the study found that both service companies and small-scale manufacturers are providing the entry-level jobs needed to combat

Leopoldo Fernández Pujals has a tempting recipe for a continent that craves jobs. A decade ago, as more Spanish women began entering the workforce, the Cuban-American marketer sensed Spain's growing appetite for fast food. So he invested \$80,000 to start a pizza-delivery service in Madrid. Now, TelePizza boasts \$260 million in sales and employs 6,000 workers. Since going public on the Spanish Bolsa in late 1996, TelePizza's shares have soared from 14 to 123, and its market cap now tops \$1.3 billion. Says Pujals, a 50-year-old Vietnam war veteran: "More and more people are asking me: 'What's our secret?'"

No wonder. At a time when Europe's industrial giants continue to shed workers, a raft of small, dynamic companies such as Pujals' are emerging. They are creating jobs and spurring economic regeneration—despite obstacles such as heavy taxes and red tape that have discouraged the Continent's entrepreneurs. Indeed, Europe's hot growth companies

are showing a remarkable ability to take advantage of the Continent's growing trend toward deregulation, its nascent secondary stock markets, and the spread of the Internet, which puts companies in instant touch with new customers. Says Juan Roure, a professor at IESE Business School in Barcelona: "These are the companies that are most effectively creating value and jobs. They are chang-

Europe's 11% jobless rate. Moreover, they aren't just clustered around tech zones such as Munich but are dotted across the Continent.

Mostly privately owned, the 500 companies identified by the study increased their employment by a total of 183,000 jobs—on average 16% annually from 1991 to 1996. At the same time, according to the study, 290 of Europe's biggest

These companies are showing a remarkable ability to take advantage of deregulation, secondary stock markets, and the Internet

ing the rules of how to compete in their markets."

Smaller growth companies have gone largely unnoticed among Europe's political elite until recently. But their continued success is vital if the Continent is to reduce the ranks of its 19 million unemployed. A new study by Europe's

companies by market capitalization slashed payrolls by 4%, or more than 500,000 jobs. The lesson, says the study's organizers, is that Europe must foster a climate that will encourage thousands more entrepreneurial companies to flourish. Says Bert W.M. Twaalfhoven, co-founder of Europe's 500:

THE HOOT THEORY

My big sister always did things a little differently, even for a big sister. Oh sure, she excelled at most of the big sister annoyances. (I remain convinced that she habitually earned good grades in school just to make me look guilty by comparison.)

Then there was the time we used a piece of chalk on the sidewalk to play tic-tac-toe. My record was 0-14-2 before I retired to the house in tears.

But what really stands out is when we were kids and she got a new bicycle. She removed the white basket with the little pink plastic flowers and both fenders even before her first trip around the block. The local gang had set up a slalom/racing course, and she wanted to compete, in both speed and style. It was immediately after her first victory that girls were forever banned from competing in future races. (That didn't

stop me from borrowing her bike and winning a few races of my own.)

So it wasn't a real surprise when, at a family gathering, my brother-in-law showed up behind the wheel of a new Catera, only directing all inquiries to my sister. "It's hers; she bought it." Figures.



Me and my brethren grilled her relentlessly. Traction control? Speed-sensitive steering? ABS? (Yes, yes, yes.) What kinda horsepower? ("24-valve V6 with 200 h.p.") Apparently she knows her stuff.

She proceeded to regale her audience with a discussion of sodium-filled exhaust valves and how it provides Catera with more horses. Male pride had us all nodding

knowingly; we could all privately consult one of the car magazines for an explanation later.

Even a simple inquiry about Catera's inside prompted a lengthy response. Something about the driver's seat "hip points" being raised for the optimum driving position. I guess I should have taken notes.

What's it like on the road? ("A hoot.") Maybe not the most descriptive of words, but there was a decided twinkle in her eye that said volumes.

What I needed was a chance to investigate this "hoot" theory a little more closely. The forgotten dinner rolls provided the perfect opportunity to volunteer for a store run.

"I think your car is blocking mine," I slyly told my sister. "No it's not," she said, as she tossed me the keys. (She still can be annoying.)

But as far as Catera being a "hoot" to drive? Well, she was right about that.



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International Business

"Philips and Siemens aren't creating new jobs in Europe. It's a whole group of hidden performers."

The No. 1 job creator in the study is Pujals' TelePizza. It increased its payroll by 62% annually from 1991 to 1996, creating 5,787 jobs over five years as its sales jumped 1,364% (table). And it's not only low-skilled jobs that are sprouting among Europe's flourishing small and midsize players. Technology companies have also been among the leading job creators in Europe. France's Gemplus—a maker of plastic cards containing an embedded microprocessor and memory chip used in phone booths and bank cards—saw its sales leap 48%, to \$569 million, last year alone as it hired 1,092 new staffers. Now, the company may go public. Although there are disadvantages to starting a company in France, concedes CEO Daniel LeGal, Gemplus owes its success to "being in a market growing 25% to 30% a year."

The surge in jobs at tech companies is expected to accelerate as Internet use continues to spread. "Growth in the

Internet has helped fuel our business," observes Christopher Horn, CEO of Ireland's IONA Technologies PLC, which sells products that help diverse software packages work together. Founded in 1991, IONA now employs 470 people. Sales more than doubled last year, to \$48 million in 1997, and some analysts see revenues hitting \$85 million this year. Last year, IONA went public on NASDAQ through an initial public offering that valued the company at \$360 million.

OPENINGS. In industries such as aviation and telecommunications, meanwhile, small growth companies are taking advantage of market openings in the European Union. Regional airlines such as Britain's Cityflyer Express Ltd. are taking off now that Europe is allowing full-fledged competition in air travel across the Continent. In telecom, Finland's Elcoteq Network has benefited from the boom in mobile phones. Once a struggling flat-panel-display maker, Elcoteq now supplies mobile phones to Nokia Corp. and L.M. Ericsson. Last year, they accounted for 70% of Elcoteq's \$303

million in revenues. The company employs 1,800 people, up from 170 in 1991.

Many European growth companies are scoring simply by answering consumers' demands for better service. Four years ago, Euro-Med opened a hotel, fitness center, beauty spa, and medical clinic near Nuremberg aimed at Europeans who want first-class health facilities at prices not much higher than those of conventional hospitals. Euro-Med plans to double its staff of doctors to 100 by 2000, says President and co-founder Wolf-Michael Wunsche.

Such success stories offer a glimmer of hope for the Continent. It will take lower taxes and more relaxed work rules to really create an environment where entrepreneurs thrive and unemployment dwindles. But Europe may be finally waking up to the fact that small companies are key to growth and prosperity.

By Julia Flynn, with Heidi Dawley, in London, Stephen Baker in Madrid, Gail Edmondson in Paris, and bureau reports

Hot Growth Across the Continent

Booming sales at small and midsize companies are fueling job creation[†]

COMPANY NAME COUNTRY	FIVE-YEAR SALES INCREASE*	DESCRIPTION	SALES ** MILLIONS OF \$	NET JOBS* CREATED
ITE GROUP BRITAIN	13,567%	International exhibition organizer	30.2	153
FIRM SECURITY GROUP BRITAIN	8,679	Security-services provider	25.8	765
SOFTWARE WAREHOUSE BRITAIN	7,714	Hardware and software supplier	23.0	204
EURO-MED GERMANY	6,567	Medical services and research	20.2	166
PACO RETAIL BRITAIN	5,457	Clothing retailer	21.6	234
BUSINESS OBJECTS FRANCE	4,659	Software development and sales	65.9	527
COFIMAN SPAIN	3,681	Hardware and software wholesaler	38.6	68
POUNDLAND BRITAIN	3,404	Housewares retailer	83.5	998
COSTCUTTER SUPERMARKETS BRITAIN	3,143	Grocery retailer and franchiser	220.9	267
IKM GROUP NORWAY	2,849	Engineering, inspection, chemical cleaning	35.8	386
DX COMMUNICATIONS BRITAIN	2,678	Communication-equipment supplier	36.9	150
ADVANCE RISC MACHINES BRITAIN	2,219	Chip designer	24.6	143
TELES GERMANY	2,100	Supplier of ISDN/PC technology	33.4	255
MERCERON MDG MCCR FRANCE	1,951	Manufacturer of road tankers	27.9	91
BERGER BAU GERMANY	1,847	Construction of ready-made houses	35.6	184
LINTEC COMPUTER GERMANY	1,762	Hardware and software wholesaler	73.5	162
ALTEC INFORMATION SYSTEMS GREECE	1,413	Personal-computer assembly and distribution	53.5	135
TELEPIZZA SPAIN	1,364	Pizza baking and delivery	163.6	5,787
AFINSA BIENES TANGIBLES SPAIN	1,348	Antique art-object wholesaler	83.9	163
CAVES DE LANDIRAS FRANCE	1,239	Wine producer and trader	63.2	135
FAULDS ADVERTISING BRITAIN	1,239	Advertising agency	35.5	72
ELCOTEQ NETWORK FINLAND	1,200	Electronic-manufacturing services	166.0	1,718
ELEMASTER TECHNOLOGIE ITALY	1,183	Design and production of electronic devices	21.6	80
CASA DAMIANI ITALY	1,119	Jewelry producer and distributor	78.7	82
LERNOUT AND HAUSPIE SPEECH BELGIUM	1,068	Voice-recognition technology	20.8	66

*1991-1996 **1996 †= sales over 20 million \$

DATA: IP STRATEGIES; EUROPE'S 500 1997 HONORARY LISTING; BUSINESS WEEK

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EDITED BY JOHN TEMPLEMAN

BRITAIN: EACH REFORM WIDENS THE GAP WITH EUROPE

Outside 10 Downing Street, a London bobby snaps a picture of his visiting family in the fabled doorway of British Prime Minister Tony Blair's official residence. Inside, past 18th century portraits in the hallway, an air of calm reigns as Blair pushes ahead with his quiet revolution. Alone among Europe's major countries, Britain is making a serious effort to tackle the twin ills of unemployment and lack of competitiveness. Increasingly, Blair seems to be the only leader who knows what he wants and how to get it. Chancellor Helmut Kohl, for instance, has failed to enact long-promised tax and welfare reforms that would reenergize Germany. And in France, Prime Minister Lionel Jospin's Socialist Party is adding labor rules, such as cutting the workweek to 35 hours, which would weaken the economy.

In the British budget to be unveiled on Mar. 17, Blair and his Chancellor of the Exchequer Gordon Brown will likely take steps that open yet a wider gap with Europe. They plan to take another crack at reforming the welfare state. Last year, Blair announced a \$5.7 billion program to help unemployed young people to work. Now, possible moves include tax credits for low income families. Brown may even halve the lowest income tax rate to 10%.

ENTREPRENEURS' CHAMPION. While Labour Party rhetoric stresses helping the poor, Blair is fascinated by the entrepreneurial verve that has created so many high-paid, high-tech jobs in the U.S. So he is looking for ways to supercharge Britain's entrepreneurial spirit. Moves under study include special tax treatment for risky investments; breaks on one-added tax to small business; and capital-gains incentives for investors to hold investments for the long term. Individually, none of the measures will amount to huge gains this year. Chancellor Brown's main priority is to keep

spending down and policy credible so that the markets will cut British interest rates—now around 6% for 10-year bonds. The thinking at Downing Street is that the best way to help entrepreneurs is to provide them with a stable macroeconomic policy “and let them get on with it,” says a Blair aide.

In many respects Britain is now the country best prepared for the rigors of European Monetary Union—even though it won't join in the first wave. Britain's tax and labor regimes are far more competitive than those of France and Germany—one reason it has attracted so much foreign investment in recent years.



BLAIR: Preaching a lonely gospel

Blair wants EMU to succeed because otherwise, he fears, economic chaos on the Continent could batter Britain. He has used Britain's current six-month presidency of the European Union to preach the reform gospel. “Labor market adaptability and flexibility will be necessary for the euro to succeed,” he said recently. “If there are uncompetitive practices, they will be exposed.”

Other EU members have agreed to study ways to get people off welfare. But just how much of Blair's message they absorb is another matter. Continental politicians, says Michael Hughes, an economist at Barclays Capital in London, are more likely to listen “to people rambling on the streets of Paris.”

Blair is playing for the long term. His main goal, for now, is to stop France and others from using the EMU to force Britain to raise its taxes and increase regulation to match Continental regimes. He has allies among reform governments taking root in smaller countries such as Holland and Denmark. Eventually, more competitive environments in those countries—as well as Britain—may force France and Germany to face global reality.

By Stanley Reed in London

GLOBAL WRAPUP

CANDAL IN SOUTH AFRICA?

South Africa's Public Protector is probing whether Deputy President Thabo Mbeki and Health Minister Mosis Maseko acted unethically by arguing that research resume on an anti-AIDS drug, Virodene. The opposition Democratic Party claims Pretoria-based Cryopreservation Technologies offered the ruling African National Congress a 6% stake in a unit that would hold patents on the drug.

An investigator at the Public Protector's office says a company docu-

ment shows a proposal to give shares was discussed internally. But a company official says no shares were ever offered to, nor was the idea discussed with, the ANC. Mbeki, Zuma, and the ANC all deny any wrongdoing, saying they tried to speed testing of the drug, banned by the Medicines Control Council because it contains a toxic industrial solvent, to help AIDS sufferers.

CGE'S BIG MEDIA AMBITIONS

► Don't count France out in the battle for global media, communications, and Internet customers. On Mar. 9,

France's \$27 billion water utility Compagnie Générale des Eaux bid to acquire French media giant Havas for \$6.5 billion. The move gives CGE a 34% stake in European pay-TV leader Canal Plus and a huge print-media empire at Havas.

With \$8 billion in media-based sales, says Chief Executive Jean-Marie Messier, the enlarged CGE will rank No. 11 globally behind the likes of Time Warner, Disney, and News Corp. Messier figures that gives CGE an entry ticket to challenge the giants—and give them a run for their money.

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To viewers watching the ad for the new Volkswagen Beetle, it is like squinting into the past. A vague image begins as a small circle set against a stark white background. As the picture sharpens, the circle becomes a flower—with seven daffodil-yellow New Beetles as its petals. The cute-as-a-Bug cars drive away, and a zippy black Beetle careens into view and skids to a stop. The tag line: "Less flower. More power."

Welcome back to the '60s—except this time, the revolution will be televised by Madison Avenue. Volkswagen's Flower Power commercial is only the first in a barrage of ads about to hit the airwaves as the German auto maker launches a new and improved version of the venerable Beetle to America after a 20-year absence. Volkswagen's strategy is simple: It plans to sell its back-to-the-future car by wrapping it in the symbols of the not-too-distant past.

Volkswagen is not the only marketer mining the warm associations of boomer youth and the Age of Aquarius to sell consumer goods. These days, nostalgia marketing is everywhere, from almost forgotten brands such as Burma Shave to jingles that borrow from classic rock. Pepsi uses the Rolling



THEN

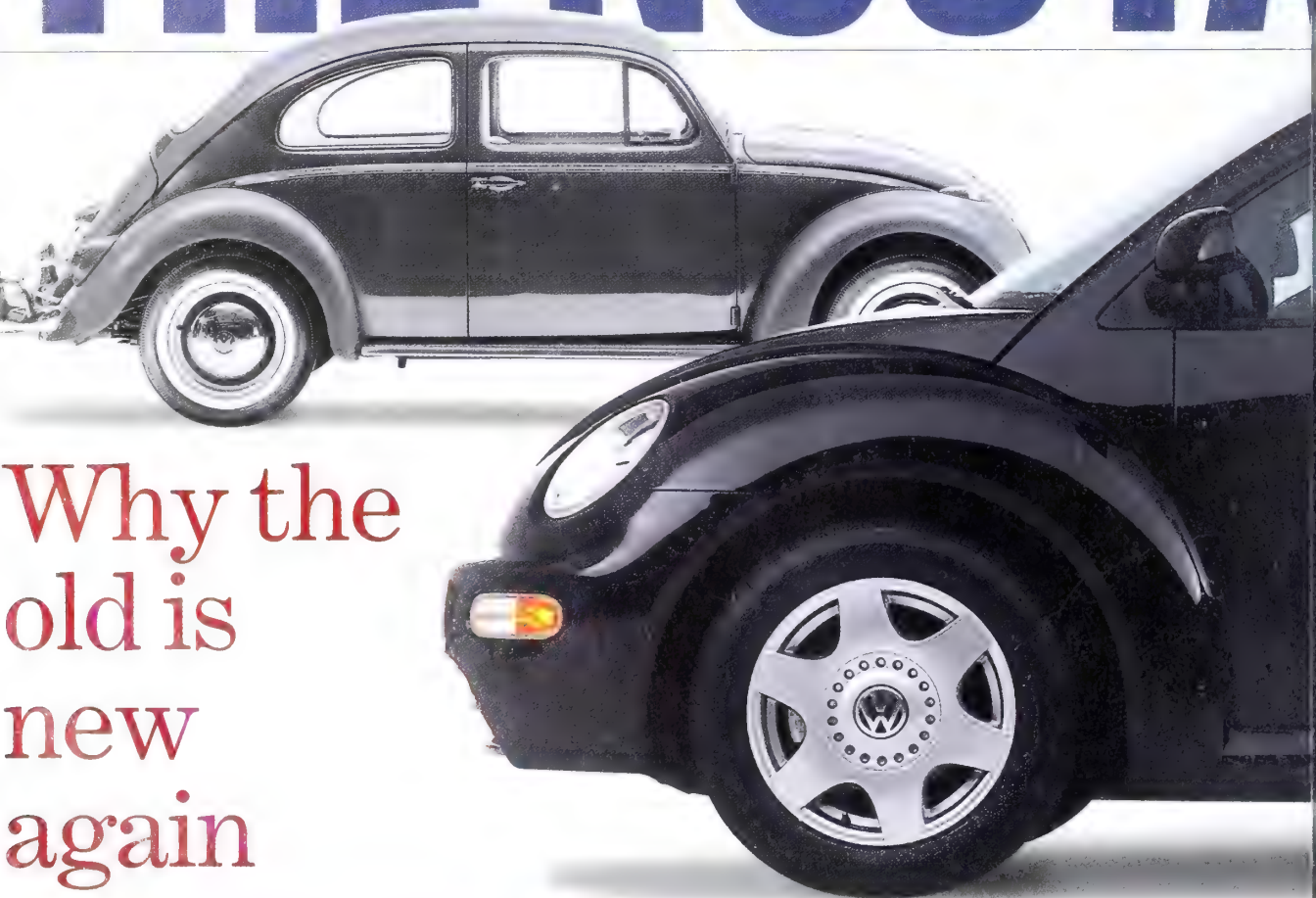
The original Bug was short on comforts but felt groovy

Stones' *Brown Sugar*, while James Brown's *I Feel Good* helps sell Senokot Laxatives. Hollywood is awash with remakes of movies and TV shows plucked from an earlier era (page 64). Even retired slogans and mascots are being resurrected. Maxwell House has dusted off "Good to the last drop," while Charlie the Tuna is swimming his way through Starkist tuna ads once again.

Consumers can't seem to get enough of these airbrushed memories. Middle-aged boomers obsessed with their youth and movin' down the highway toward retirement clamor for retro roadsters such as the Porsche Boxster. Walt Disney Co. developed an entire town, Celebration, Fla., on the notion that Americans are pining for the look and feel of 1940s neighborhoods. Baseball fans step back in time by piling into Cleveland's Jacobs Field and Oriole Park at Camden Yards—new ballparks designed to look like they've been around since the turn of the century. Meanwhile, kids have reclaimed mom and dad's bell bottoms and platform shoes and brought back Diane Von Furstenberg's wrap dress.

No one, though, has as much riding on the nostalgia wave as Volkswagen. Its U.S. market share having withered to less

THE NOSTA



Why the old is new again

1%, vw is wagering \$560 million that its tiny little car can revive its fortunes. It's a calculated bet. The new, postmodern Beetle has been reinvented with a message that slyly eases end-of-the-millennium angst with a harken-back to the Summer of Love. The new version, which is about to hit the showrooms, comes with all the modern features car buyers demand, such as air bags and power outlets for cell phones. That's not why vw expects folks to buy it. With its familiar bubble shape that still makes people smile and skitters by, the new Beetle offers a pull that is very emotional. "If you sold your soul in the '80s," says one ad, "here's your chance to buy it back."

SS RELIEF? Why the intense yearning to turn back the clock? The faster we hurdle toward the 21st century, it seems, the more we're reaching desperately backwards toward the halcyon days of mid-century, of postwar prosperity and quaint notions of revolution. Nowadays seem astonishing in their innocence and idealism. In their place have come growing anxiety about aging and fear of hanging on in today's increasingly stressful society. Americans are overwhelmed, social experts say, by the onslaught of the Information Age, with its high-



NOW

The '98 Beetle wraps new tech in an evocative package

speed modems, cell phones, and pagers. While we hail the benefits of the wired '90s, at the same time we are buffeted by the rapid pace of change. "We are creating a new culture, and we don't know what's going to happen," explains futurist Watts Wacker, co-author of *The 500-Year Delta*. "So we need some warm fuzzies from our past."

Just take a stroll through the supermarket. Shelves are now brimming with packaged goods that look as if they're from another era. After Coca-Cola Co. recreated a plastic version of its famous contour bottle in 1994, sales grew by double digits in some markets, says Frank P. Bifulco, vice-president for marketing of Coca-Cola USA. Necco wafers are enjoying a comeback—sales are up 25% in the past two years—thanks in part to a packaging redesign that harkens back to its roots. "There has been a

flurry of clients coming to us and saying, 'We want that handcrafted look,'" says Jack Vogler, partner at SBG Enterprise, a San Francisco packaging-design house that recently restored the old packaging of the Sun-Maid raisin girl and Cracker Jack's Sailor Jack and Bingo.

Even old ads are being recycled to woo wistful customers. Sales of Maxwell House have perked up since it began in-

GLIA BOOM

Cover Story





STARKIST

Sorry, Charlie: The tuna has been coaxed out of retirement for new TV spots



wagon—even when they don't have archives to pillage. In February, Ford Motor Co. began airing a commercial commemorating how Henry Ford put America on wheels. The spot includes what appears to be grainy, historic footage of a Model T putting down a long-ago Main Street. But the sepia-toned scene was actually shot last year on a Hollywood back lot and was given a vintage look by using a 1920s hand-cranked camera, old emulsion film, and special editing.

Why recreate history? Ford is hoping that consumers will

equate longevity with quality. "People really respond to it. They say, 'This is a compa-

ny that has lasted through a couple of world wars,'" says Bruce Rooke, executive creative director at Ford's agency, J. Walter Thompson Co.

Indeed, social experts say much of the appeal of nostalgia stems from a longing for a return to simpler times. Despite a robust economy, Americans remain an anxiety-ridden bunch. Not all the riches of a long bull market can make up for the rigors of overbooked working parents forced to reduce family life to an exercise in time management. Divorce rates remain high, job security is down, and saving enough to send the kids to college or for retirement can seem overwhelming. Is it any wonder that a new survey from Roper Starch Worldwide shows that 55% of Americans believe the "good old days" were better than today? That's an about-face from attitudes of a generation ago, when 54% of those surveyed in 1974 told Roper they believed there was no time better than the present.

GOLDEN MEMORIES. Naturally, baby boomers, ever powerful in their numbers, are driving this return to roots. The Roper survey identifies the most longed-for age as the 1950s, 1960s, and 1970s. "The '50s and '60s were a time of very high expectations for baby boomers," says J. Walker Smith, a partner with the Yankelovich Partners consumer-research firm. "But life didn't turn out to be the 1964 World's Fair."

In fact, life went on, and aging is yet another force at the root of nostalgia marketing. The oldest

cluding archival footage of percolating coffee pots in its ads. It's a startling departure from the modern image Maxwell House projected in the early 1990s as hip upstarts such as Starbucks Corp. became all the rage. "Consumers are not in a real experimental time now," says Richard S. Helstein, vice-president for advertising at Kraft Foods Inc. "They are looking for brands they can depend on—brands they grew up with."

Successes such as these have advertisers jumping on the band-

Cover Story

KFC

The colonel's face looms large again



Even today's youth

are adopting icons



A&W RESTAURANTS

The entire chain has flipped for a 1950s ambience that, as one customer says, "reminds you of your youth"

of the boomers are in their 50s and are resisting the aging process with the vigor they once reserved for protesting the war. While they snap up vitamins, diet pills, and other tonics touted to stop the clock, marketers are counting on the appeal of nostalgic products to salve the wounds of growing old. If nothing else, familiar products and jingles give boomers the chance to act and feel young. "Boomers are saying 'Maybe my parents were old at 50, but I'm not,'" says Rick Adler, president of Senior Network Inc., a marketing consultant firm.

That's certainly a big reason why Dennis J. Berger, 52, waited six months to take delivery of his white \$65,000 Porsche Boxster, a retro roadster styled like the 1950s vintage Porsche favored by movie stars like James Dean. "It opened up a memory of when I was a teenager in New Jersey," says Berger, vice-president of Allied Plastics Co. in Jacksonville, Fla. "This car reminds me of the '50s, when there wasn't a care in the world."

Yet the nostalgia phenomenon is not simply about America reliving a Golden Age. It is also about reinterpreting it. We may look back through rose-colored glasses, but few want to live in the past for the sake of authenticity. The new retro ethos has a thoroughly modern



COCA-COLA

A familiar contour gave sales a lift

cast. Log Cabin syrup brought back an old-timey label but sports a convenient squeeze-

bottle. When Coke redid its famous hourglass bottle, it e it in today's popular big-gulp sizes. And movie res come complete with the latest in special effects. Americans want that Victorian house with the wraparound n, but it had better be wired for all the latest technology," Carolyn E. Setlow, senior vice-president at Roper. Each reinterpretations are particularly popular among ger, Generation-X consumers. While they've adopted y products and fashions from the 1960s and 1970s as own, they often update them with an ironic twist. And s little to do with longing for an era they never experi- d. "I see it more as rediscovering than retro," says 20- old Matthew Levy of New York City. "I don't want to be ather. I want to rediscover things he forgot about when as out climbing the corporate ladder." Case in point: s. Both he and his dad smoke them. But Levy says his ration has reinvented the product to suit its lifestyle. ere my dad smoked cigars, they didn't allow women. ne my age would go for that."



CRACKER JACK

Sailor Jack and Bingo stand tall again



OLD NAVY STORES

Ancient pickups and such gave "credibility to the brand, so that it didn't feel like it was coming from nowhere"

BURMA SHAVE

The old signs will soon reappear on the roads



SUN-MAID

A Frisco design firm restored the California girl's image

The vintage-style stadiums that have risen across the country embody this marriage of past and present. Camden

Yards and Jacobs Field look like ballparks from a bygone era. Coming to New York might be a recreation of the old Brooklyn Dodgers' home turf, Ebbets Field. But this time, it would house the New York Mets. On the inside, these faux-historic stadiums are ringed with the luxury suites that make corporate customers comfortable and owners rich. Even regular fans are rewarded with wider seats and broad concourses dotted with more concession stands and restrooms than real old ballparks ever had. "People will go to see a place once because it's historic," says HOK Sport Senior Vice-President Joseph E. Spear, the architect of Camden Yards and Jacobs Field. "But they don't come back unless they have a good time."

POWER SUNROOF. The Beetle comeback is also based on a combination of romance and reason—wrapping up modern conveniences in an old-style package. Built into the dashboard is a bud vase perfect for a daisy plucked straight from the 1960s. But right next to it is a high-tech multi-speaker stereo—and options like power windows, cruise con-

time before most of them were born

trol, and a power sunroof make it a very different car than the rattly old Bug. So, too, does the sticker price: While a new Bug cost just \$1,800 in 1968—\$8,300 in today's dollars—a typically equipped new Beetle will run about \$16,500.

But if the Beetle, like us, has grown up, Volkswagen is hoping it will still spark the same emotions as its younger self. With its simple design and no-frills engineering, the original Beetle was the antithesis of Detroit's gas-guzzlers. As boomers by the tens of thousands bought their first cars, it blossomed into an unlikely icon. By 1968, its peak year, vw sold 423,000 Beetles in the U.S. Cheap to own, easy to fix, and giddy fun to drive, the Beetle personified an era of rebellion against conventions. Says John Wright, a pop-culture expert at the Henry Ford Museum in Dearborn, Mich.: "When people look at Volkswagen, it looks like youth."

But youth fades, and by the late 1970s, the Bug had faded, too. vw was never the same after it dropped the Beetle from production for the U.S. in 1978. By 1993, says Jens Neumann, a member of Volkswagen's board of managers, with less than 1% of U.S. auto sales, "we were just about to drop out of this market."

MYSTERY MARKET. Instead, vw Chairman Ferdinand Piëch decided to make an almost quixotic bid to recapture its former glory. In 1993, he ordered up a prototype of a new Beetle in

what was essentially a last-ditch effort to jump-start sales. The concept car was

launched at the 1994 auto show in Detroit—and promptly stole the show as car shoppers and reporters mobbed the vw display. Crowds packed in several people deep just to get a look at the yellow Bug. The wildly enthusiastic reaction from the public astounded even vw execs. "We were, to say the least, overwhelmed," says Piëch.

Still, vw is walking softly into the market. It plans to build just 100,000 Beetles a year at its plant in Puebla, Mexico, with half of those targeted for the U.S. and Canada. Company ex-



ecs refuse to be pinned down on the Beetle's target market, saying only that it is designed for "optimists." Yet it's clearly aiming wide. While many of its ads sport jokes targeted at the previous Beetle generation, others are aimed squarely at Gen-X.

VIACOM One oldies channel just wasn't enough: After Nick at Nite came TV Land

from 100 customers. "It's like you have a rock star here and everybody wants an autograph," La Plant says. "I've never seen a car that had such a wide range of interest, from 16-year-olds to 65-year-olds."

Greg Stern, a 47-year-old film producer in Santa Monica, is No. 1 on La Plant's list. Describing the car as—what else—"way cool," he's in line for a silver or white model. "In 1967, my Dad got me a vw. I loved it. I'm sure the new one will take me back," says Stern. "I'm getting the New Beetle as a surprise for my daughter, but I'm sure I'm going to be stealing it from her all the time."

Like Volkswagen, others have discovered that a history of warm memories is an exploitable asset these days. The Nickelodeon cable channel's Nick at Nite proved such a hit recycling sitcoms that it spawned TV Land and a host of other imitators. That's true even if the product itself has been gone for decades. Burma Shave is banking almost entirely on its nostalgic appeal as it returns to store shelves after a 30-year absence. The shaving cream's legendary rhyming roadside signs last seen in 1964, will return this summer. And they may even begin showing up in the supermarkets and Wal-Marts where Burma Shave is now sold, says brand manager Steve Cochran. "Those signs evoke a lot of nostalgia about driving along the highway on vacation," he says.

At least Burma Shave's history is real. As nostalgia becomes ever more important as a marketing tool, companies are increasingly willing to fake it. Four years ago, Gap Inc. launched the Old Navy casual clothing chain with a series of

Cover Story

Rock On!

In the battle to win the hearts and minds of aging boomers, more and more marketers are turning to old rock and pop hits



THE BEE GEES



JAMES BROWN

BRAND	ARTIST	SONG
Toyota	Sly and the Family Stone	<i>Everyday People</i>
AT&T	Elton John	<i>Rocket Man</i>
Senokot Laxative	James Brown	<i>I Feel Good</i>
Pepsi	The Rolling Stones	<i>Brown Sugar</i>
Microsoft	The Rolling Stones	<i>Start Me Up</i>
Ford	The Who	<i>I Can't Explain</i>
Intel	Bee Gees	<i>Stayin' Alive</i>
Levi's	The Partridge Family	<i>I Think I Love You</i>
Burger King	Squeeze	<i>Tempted</i>



MICK JAGGER



timey black-and-white ads and store fronts that recalled the '50s. The used nostalgia in the beginning gave credibility to the brand, but it didn't feel like it was coming from nowhere," says Richard Crisman, Old Navy's senior vice-president for marketing. Since then, Old Navy has modernized its marketing with new campaigns emphasizing value and fashion. But many of the original decor touches remain—all 300 stores have a '50s Chevy pickup truck, for example, and the New York flagship store features a '50s-style diner.

MA FLOP. For Old Navy, the tactic paid off. But not all efforts to manufacture nostalgia have been so successful. Excessives at fast-food chain Kentucky Fried Chicken Corp. proved that you can go too far. Three years ago, they decided the brand needed some advertising help from founder Colonel Sanders. KFC's research showed that customers still trusted the colonel. The problem: Sanders died in 1980, and KFC could not find old film clips of him that would work in a modern commercial. "Nothing was sound-bite enough," explained Peter J. Foulds, KFC's advertising vice-president.

KFC dressed up an actor in the colonel's trademark white suit and broadcast black-and-white TV commercials that pretended to show the founder spouting his special brand of spun wisdom. But the attempt to recreate history didn't wash, and KFC was roundly criticized for defaming the dead. After less than a year, the ads were pulled. Still, KFC hasn't given up on using the colonel alto-



NECCO WAFERS

Retro packaging has helped send sales up 25%

CAMDEN YARDS

Takes 'em back to a 1900s ballpark—at least in spirit

to endorse products is sophisticated technology. Computer-generated imagery has made it appear that Fred Astaire had a new dancing partner—Dirt Devil vacuum cleaners. Lucille Ball sells diamond rings for Service Merchandise Co. And Ed Sullivan is back from the beyond to unveil one more phenom to the world: the Mercedes-Benz sport-utility. "Who is Mr. Introduction-to-America more than Ed Sullivan?" says Mike Jackson, president of Mercedes-Benz of North America.

If only reviving a dying brand were as easy. A&W Restaurants Inc., once famous for carhops on roller skates, is attempting to reverse more than two decades of decline by overhauling its restaurants in a 1950s rock 'n' roll image. A&W Chairman Sidney Feltenstein, a former Burger King Corp. marketing executive, hopes the retro appeal will help them stand out in a crowded segment. Feltenstein says McDonald's Corp. and Burger King can fight

over the kids; he's aiming for adults. So far, the makeover appears to be working: At one redone A&W in Dearborn, Mich., middle-age diners dominate the lunchtime crowd. "It reminds you of your youth," says salesman Kirk Pettit, 38, as Beach Boys music wafts from an old Wurlitzer jukebox. Overall, sales at the remodeled stores are up 20% over 1996.

So is nostalgia just the latest hype from Madison Avenue? Or is it the zeitgeist of a culture? While it clearly hits a chord, some worry that



DIRT DEVIL

Fred Astaire hooks up with the Broom Vac

Too much of a good thing? Ad shops fear overkill

overkill can't be far off. "The grainy black-and-white commercials are the shaky camera of the late '90s," scoffs Martin Horn, Chicago-based research director at DDB Needham Worldwide Inc. "We in the ad business slide into derivative behavior." Also dubious is John K. Grace, executive director of Interbrand, a New York-based brand consultancy, who believes American culture in the late '90s lacks distinction, so young and old alike are clinging to the sights and sounds of the past

Cover Story

until something better comes along. He compares it to the quiet 1950s, which led to the tumultuous 1960s: "There are no cultural hooks for youth to grab on to today, so they find comfort in what was. But nostalgia can't be sustained."

But others say advertisers are only reflecting Americans' deeper longings to take control of their lives by reconnecting with their idealized past. "If you want to understand values,

study our advertising," says Seymour Leventman, a sociology professor at Boston College. He believes the nostalgia craze will only grow as trend-setting baby boomers age.

That's why the New Beetle just might be a tonic for the times. It is our romantic past, reinvented for our hectic here-and-now. "The Beetle is not just empty nostalgia," says Gerald Celente, publisher of *Trends Journal*. "It is a practical car that is also tied closely to the emotions of a generation."

To unleash that emotion, vw's staid German executives flew to Atlanta to stage a love-in to introduce the Love Bug last month to 300 journalists from around the world. Young women in tie-dyed T-shirts handed out daisies and peace medallions in a psychedelic rock hall. vw's Piëch marveled at his little car's enduring appeal. "It is different, and it makes you feel different," he said. "It's like a magnet." Different, yet deeply familiar—a car for the times.

By Keith Naughton and Bill Vlasic in Detroit, with bureau reports

HEY, IF IT WORKED BEFORE...

His goofy bowl-cut hairstyle is gone, and the suit is blue instead of red. But six years after ending a 35-year TV run, Captain Kangaroo is back—and so are Mr. Greenjeans and Mr. Moose. Starting last fall, a recast Captain welcomed a new generation of preschoolers to the Treasure House.

As they say in Hollywood: When in doubt, recycle. Although remakes and sequels have always played a big role in Tinseltown, never before have so many producers devoted so much time to story lines pilfered from the past. "Just about every studio is dredging up something from its library," says Dean Devlin, producer of the upcoming *Godzilla* movie.

WARM MEMORIES. In the past three years alone, Universal has made big, live-action movie hits out of *The Flintstones* and *Casper*. Walt Disney Co. had a smash in the live-action updating of *101 Dalmatians*. Plenty more is on the way, including summer films based on the '60s shows *Lost in Space* and *The Avengers*. Meanwhile, TV remakes of *The Love Boat*, *Fantasy Island*, and *The Hollywood Squares* are in the works. This month, Paramount will re-release *Grease*.

Why the deluge? Larry Jones, general manager of Viacom Inc.'s Nick at Nite and TV Land oldie channels, believes it "reflects a need for people to get back to a time when

life was simpler." Jones should know: The highly successful diet of *Hogan's Heroes* and *I Love Lucy* reruns his channels serve up has launched a host of copycats.

But warm memories are just part of the trend. Another prime driver is money. The film and TV industry spends millions each year developing

Bilko, and *Mr. Magoo*. In February, Universal Pictures flopped with a sequel to the 20-year-old *The Blues Brothers* movie. These failed largely because they didn't offer anything new. "It can't look so much like the original that it looks like it should be on late-night TV," says Devlin.

Indeed, Hollywood is discovering that remakes require plenty of modern-day gimmickry. Paramount Pictures turned *Mission: Impossible* into an \$189 million blockbuster by signing Tom Cruise and loading the film with special effects. The studio's 1996 film of *The Brady Bunch* scored by portraying the wholesome, bell-bottom-clad 1970s family as 1990s misfits. "You have to have a unique gimmick or people aren't going to buy your film no matter how familiar they might be with it," says *Brady Bunch* producer Alan Ladd Jr.

That's why King World Productions Inc. paid a reported \$3 million bonus to get Whoopi Goldberg to sit in the center square for its redo of the game show *The Hollywood Squares*.

To turn Generation Xers onto their *Lost in Space* movie, New Line Cinema hired popular actors such as *Friends*' Matt LeBlanc.

To see how oldies can work in the right setting, just look at CBS: Catering to its aging boomer viewers, it has boosted Friday ratings by adding new versions of *Candid Camera* and *Kids Say the Darndest Things* to the lineup. It's tried. It's true. Best of all, it packs the house.

By Ronald Grover in Los Angeles



TIME TRAVEL

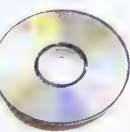
The new *Lost in Space* has big stars, pricey effects

projects that never make it to the screen. A remake or sequel is a known quantity that many in the

increasingly risk-averse industry assume will have built-in audience appeal.

Still, not all oldies are reborn as goodies. Last year's Tinseltown bombs include movies based on *McHale's Navy*, *Flipper*, *Sergeant*

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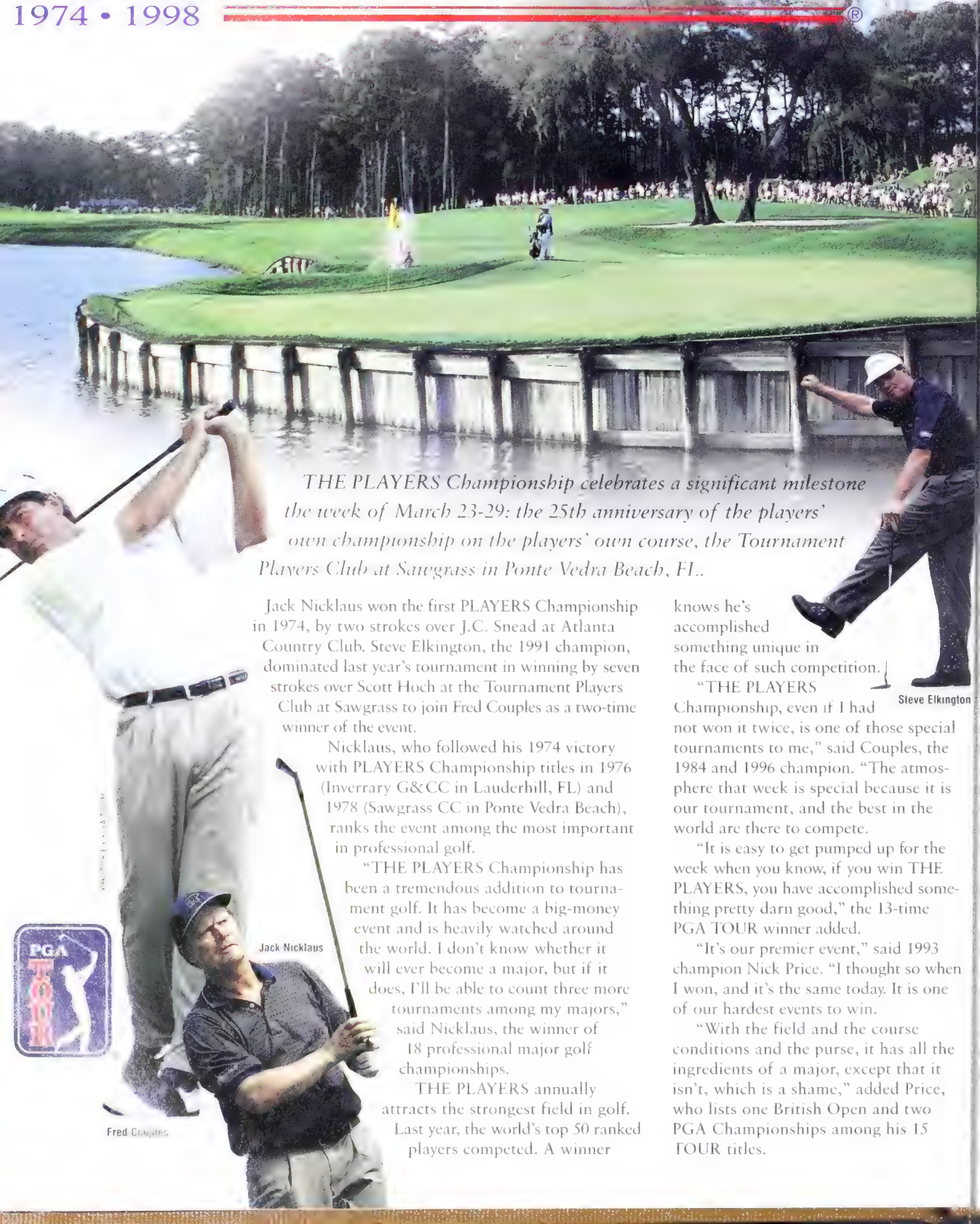
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25
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THE PLAYERS

CHAMPIONSHIP



THE PLAYERS Championship celebrates a significant milestone the week of March 23-29: the 25th anniversary of the players' own championship on the players' own course, the Tournament Players Club at Sawgrass in Ponte Vedra Beach, FL.

Jack Nicklaus won the first PLAYERS Championship in 1974, by two strokes over J.C. Snead at Atlanta Country Club. Steve Elkington, the 1991 champion, dominated last year's tournament in winning by seven strokes over Scott Hoch at the Tournament Players Club at Sawgrass to join Fred Couples as a two-time winner of the event.

Nicklaus, who followed his 1974 victory with PLAYERS Championship titles in 1976 (Inverrary G&CC in Lauderhill, FL) and 1978 (Sawgrass CC in Ponte Vedra Beach), ranks the event among the most important in professional golf.

"THE PLAYERS Championship has been a tremendous addition to tournament golf. It has become a big-money event and is heavily watched around the world. I don't know whether it will ever become a major, but if it does, I'll be able to count three more tournaments among my majors," said Nicklaus, the winner of 18 professional major golf championships.

THE PLAYERS annually attracts the strongest field in golf. Last year, the world's top 50 ranked players competed. A winner

knows he's accomplished something unique in the face of such competition.

"THE PLAYERS

Championship, even if I had not won it twice," said Couples, the 1984 and 1996 champion. "The atmosphere that week is special because it is our tournament, and the best in the world are there to compete.

"It is easy to get pumped up for the week when you know, if you win THE PLAYERS, you have accomplished something pretty darn good," the 13-time PGA TOUR winner added.

"It's our premier event," said 1993 champion Nick Price. "I thought so when I won, and it's the same today. It is one of our hardest events to win.

"With the field and the course conditions and the purse, it has all the ingredients of a major, except that it isn't, which is a shame," added Price, who lists one British Open and two PGA Championships among his 15 TOUR titles.

Steve Elkington

Jack Nicklaus

Fred Couples





THE PLAYERS Championship is the TOUR's showcase event," said TOUR Commissioner Tim Finchem. Since its arrival at the TPC at Sawgrass in 1982, the tournament has evolved into one of the golf world's great events. It's the year's strongest field

and one of the game's best courses annually. It's a chance for an outstanding championship. Deane Beman, the PGA TOUR can be justifiably proud of THE PLAYERS Championship." Beman, the TOUR's president and Commissioner, is credited with many of the changes for THE PLAYERS Championship, which was moved to a different course in 1977. In its first three years, it was beginning a five-year run at Sawgrass Country Club.

"I felt the TOUR needed a permanent site and roots somewhere," said Beman, who served as Commissioner from 1974 to 1994. "Secondly, the way to build THE PLAYERS was the TOUR's most important tournament was to own and control our own course and build a facility that was better than what anyone else had.

"I also felt the TOUR had benefited so much from everybody else's innovations, and here was a chance for the TOUR to be innovative," Beman added.

The result was the TPC at Sawgrass and its Stadium Course, which was unveiled to the world at the 1982 PLAYERS Championship.

Winner Jerry Pate baptized the facility in unusual fashion, propelling Beman and course architect Pete Dye into the lake adjoining the 18th green before joining them himself.

The 1998 PLAYERS offers a \$4-million purse and \$720,000 first prize. But no matter who captures the top prize at the 25th Anniversary PLAYERS Championship, the event's biggest winner will be charity.

Last year's PLAYERS Championship generated a total of \$678,000 for Northeast Florida charities,

raising its overall total to almost \$8 million. All told, PGA TOUR tournaments have raised nearly \$340 million for worthy local causes since the first donation was made in 1938.

THE PLAYERS Championship Television Schedule

Thursday, March 26
First Round
of Competition, ESPN
10:00 a.m.-1:00 p.m. EST
3:00-6:00 p.m. EST

Friday, March 27
Second Round
of Competition, ESPN
10:00 a.m.-1:00 p.m. EST
3:00-6:00 p.m. EST

Saturday, March 28
Third Round
of Competition, NBC
2:00-6:00 p.m. EST

Sunday, March 29
Final Round
of Competition, NBC
3:00-5:30 p.m. EST

THE PLAYERS Championship Results

Atlanta CC, Atlanta, GA

1974 **Jack Nicklaus**
Two strokes over J.C. Snead

Colonial CC, Fort Worth, TX

1975 **Al Geiberger**
Three strokes over Dave Stockton

Inverrary G&CC, Lauderhill, FL

1976 **Jack Nicklaus** (2)
Three strokes over J.C. Snead

Sawgrass CC, Ponte Vedra Beach, FL

1977 **Mark Hayes**
Two strokes over Mike McCullough

1978 **Jack Nicklaus** (3)
One stroke over Lou Graham

1979 **Lanny Wadkins**
Five strokes over Tom Watson

1980 **Lee Trevino**
One stroke over Ben Crenshaw

1981 **Raymond Floyd**
Won playoff over Barry Jaeckel and Curtis Strange

TPC at Sawgrass, Ponte Vedra Beach, FL

1982 **Jerry Pate**
Two strokes over Brad Bryant and Scott Simpson

1983 **Hal Sutton**
One stroke over Bob Eastwood

1984 **Fred Couples**
One stroke over Lee Trevino

1985 **Calvin Peete**
Three strokes over D.A. Weibring

1986 **John Mahaffey**
One stroke over Larry Mize

1987 **Sandy Lyle**
Won playoff over Jeff Sluman

1988 **Mark McCumber**
Four strokes over Mike Reid

1989 **Tom Kite**
One stroke over Chip Beck

1990 **Jodie Mudd**
One stroke over Mark Calcavecchia

1991 **Steve Elkington**
One stroke over Fuzzy Zoeller

1992 **Davis Love III**
Four strokes over Ian Baker-Finch, Phil Blackmar, Nick Faldo and Tom Watson

1993 **Nick Price**
Five strokes over Bernhard Langer

1994 **Greg Norman**
Four strokes over Fuzzy Zoeller

1995 **Lee Janzen**
One stroke over Bernhard Langer

1996 **Fred Couples** (2)
Four strokes over Colin Montgomerie and Tommy Tolles

1997 **Steve Elkington** (2)
Seven strokes over Scott Hoch

SOCCER

DOES MAJOR LEAGUE SOCCER HAVE LEGS?

The new season could be crucial as it struggles for acceptance

A new TV ad for Major League Soccer shows six players wildly celebrating goals they just scored. They peel off their jerseys and strut to the sound of striptease music. Emotion so overcomes one player that he falls to his knees to thank the heavens.

Unfortunately for MLS, which kicks off a new season on Mar. 15, too few of these moments occur in real life. Soccer remains one of the lowest-scoring and lowest-rated TV sports in America. Following in the footsteps of previous failed U.S. soccer leagues, MLS has lost \$40 million in its first two seasons. Though it had a surprisingly strong inaugural year, drawing 3.1

million fans, MLS attendance had dropped 16% by the end of 1997—and it could get worse: This summer's World Cup will draw attention away from MLS and possibly exacerbate the slump. As if that weren't troubling enough, MLS is being sued by players disgruntled over their relatively low pay. It all begs the question: Is pro soccer just a bad fit for a nation of sports fans with short attention spans?

Of course, soccer is still the most popular sport in the rest of the world. And "soccer moms" became part of the political lexicon in 1996 because American kids have embraced the game so enthusiastically. But professional soccer has never taken root in

the U.S. as a major league sport. In the past,

U.S. leagues were always financed one season at a time. None ever secured a TV deal. The longest surviving, the North American Soccer League, ran from 1967 to 1985 but was a dumping ground for second-tier European players. It flourished only when Brazilian great Pelé played for the New York Cosmos in the 1970s. More typical was the 14-season Major Indoor Soccer League, which folded in 1992. Only 1 of 40 teams that played in that league ever made a profit.

MLS is trying hard not to be as bush-league, but it's not easy. Just 10% of its players have a shot at making a World Cup roster this summer, says MLS Commissioner Douglas G. Logan. "American soccer is a level below our top division," gloats David Endt

of Amsterdam's Ajax Football team, one of Europe's best. "No one dreams of going to play in the U.S."

If they did, they wouldn't be allowed to, anyway. MLS limits international players to five per roster and may lower that number to four. That means more Americans get a shot at gaining world-class experience. But it also prohibits top international talent from improving the overall quality of play. Currently, most of the international players MLS attracts are unproven youngsters placed in markets with high concentrations of immigrants from their respective countries. **PAY PIQUE.** Because of its structure, MLS probably couldn't afford top-tier foreign players even if it wanted them. MLS operates like a franchise system: The league owns the teams, caps salaries and prohibits free agency. The average MLS salary is \$83,000, and the minimum a scant \$24,000. "We don't have superstars. Our players drive Honda Civics," brags Brian I. O'Donovan, general manager of the New England Revolution.

Apparently, that's not good enough for MLS players: They have filed a federal antitrust class action against the league that is scheduled to go to trial this fall. They want to be paid more in line with European-league players, who command between \$300,000 and several million dollars per season. "I'm shocked they're suing, as opposed to collectively bargaining," says Alan Rothenberg, the founder and chairman of MLS. He would prefer to see the players form a union. But if they did that they would forfeit their right to sue on antitrust grounds, says John Kerr, executive director of the MLS Players Assn. "The players just want a free market with the ability to negotiate—anything but this scam."

Even the backbone of the league—the growing U.S. Hispanic market—is proving unreliable. Hispanic attendance dropped 10% last year. To reignite that market, the league has hired Dieste

EMPTIER STANDS

Major League Soccer is having trouble hanging on to fans

YEAR	AVERAGE ATTENDANCE*	BIGGEST DROPS	
		LOS ANGELES GALAXY	N.Y./N.J. METROSTARS
1996	17,416	462,655	382,360
1997	14,616	330,010	270,388

*Average attendance at 160 regular-season games played by the 10-team league

DATA: MAJOR LEAGUE SOCCER

CRYING FOUL: MLS players have filed a suit demanding salaries in line with Europeans'

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*MSRP after \$1,000 cash back includes destination. Excludes tax. www.chryslercars.com

Partners, a Dallas-based ad agency that specializes in Hispanic marketing. But in the meantime, MLS has reduced the number of Sunday games this season by almost 25%. That could prove to be a blunder with Hispanics, for whom soccer is a Sunday ritual. MLS also miscalculated that Hispanics would purchase season tickets. "We now know they're more spontaneous and aren't as likely to buy a package," admits Logan, a former Mexico City concert promoter.

SUMMER SWEAT. This summer's World Cup, which will be held in France from June 10 to July 12, could "bury us" for a month, admits Rothenberg. But MLS is playing through. While the eyes of the world follow their favorite national teams—playing a level of soccer above that of the MLS—the U.S. league will stick with a slightly reduced schedule.

Despite those possible negatives, the league says it's on course to sell more season tickets this year than it did in '96, its first and best year. It expects expansion teams in Miami and Chicago—where there are large Hispanic contingents—to give slumping league attendance a boost. And it's crossing its fingers that the major-market New York/New Jersey MetroStars won't finish in the basement of the Eastern Conference standings again this year.

Besides securing \$80 million in sponsorship money over a five-year period, MLS's major coup to date is a guaranteed \$5 million TV deal with ABC and ESPN that will beam 47 of its 210 games into U.S. homes. That's still small change compared with ABC's \$25 million deal to broadcast all 64 World Cup games to the States this summer. But it's better than making zilch on a TV deal, which MLS did the past two seasons.

To become the fifth major sports league in this country, as MLS fashions itself, league officials know they must secure higher-paying TV deals. They also must make more than a measly \$2 million off licensing, which was all they mustered last year. As it stands, MLS relies primarily on ticket sales—a formula that killed other soccer leagues. "We've got a good baseline of support, but it might take another 10 years for this to work," says Rothenberg.

MLS Commissioner Logan is preparing for a \$20 million loss in '98. Fortunately for him, though, \$20 mil here and there doesn't seem to deter the league's backers, who include billionaires John Kluge, Philip F. Anschutz, and Robert K. Kraft. In recent meetings, backers have reportedly assured Logan that "nothing's terminal." But a legitimate major league must survive the nation's fickle remote control, where history is just a click away.

By Brad Wolverton in Atlanta

Media

THE INTERNET

NEW-MEDIA MELTDOWN

How a big online newspaper venture bit the dust

It was created with a name most of its owners disliked, with a logo one partner "hated," in a city everybody rejected, with a mission nobody understood. So it was fitting that when New Century Network was kicked off last April by nine media giants teaming up to conquer electronic competition, even the launch party bombed.

In a ballroom at the Newspaper Association of America convention in Chicago, a thousand bottles of champagne emblazoned with "New Century Network: The Collective Intelligence of America's Newspapers" awaited the hordes expected to come to toast the watershed new-media joint venture. When fewer than 100 people showed up, Chief Executive Lee de Boer made an abbreviated speech before retreating. "They built a business and nobody came," says David Morgan, president of the online ad agency Real Media Inc.

The reception was the first public humiliation for New Century Network, but only one in a series of blunders that culminated in the company's abrupt shutdown on Mar. 10. Created in 1995 to unite newspapers against Microsoft Corp. and other competitors girding to woo electronically advertisers and readers, New Century Network came to embody everything that could go wrong when old-line newspapers converge with new media. "Newspapers are reacting in

very traditional ways to a very untraditional marketplace," says Peter M. Winter, president of Cox Interactive Media, who was New Century Network's original chief executive. "And they're being superceded fast."

Started with \$1 million each from Knight-Ridder, Tribune, Times Mirror, Advance Publications, Cox Enterprises, Gannett, Hearst, Washington Post, and New York Times, New Century seemed an entrepreneurial dream. The Internet had just

opened to the world, creating vast new competition for readers—and for the advertisers that pump \$40 billion into newspapers. But it also gave newspapers a chance to capture national accounts that favored the one-stop-shopping convenience of TV and national magazines.

CUMBERSOME. And New Century had something even William H. Gates II coveted: the content of newspapers throughout the country. Affiliates could use Mardi Gras stories from the *New Orleans Times Picayune* or Hollywood news from the *Los Angeles Times*. Separate subject-oriented Web sites would pool stories on everything from health

NEW CENTURY: A HOUSE DIVIDED

Nine media companies created New Century Network to link 140 newspapers online. But the venture was paralyzed by constant clashes. Some results:



- ▶ Took 18 months to find a chief executive
- ▶ Killed a plan to go public
- ▶ Failed to run lucrative classifieds
- ▶ Created a news Web site that competed with large papers
- ▶ Failed to promote site
- ▶ Generated little traffic and ad revenue



to sports. And advertisers could
anners on one site or 100 with the
of a button.

t the media companies had wildly
ging philosophies about how news-
s should make the electronic leap
what role the new venture should
"You had private companies and
e companies and companies that
risk-averse and those that were
tolerant," says Harry Chandler, head
w media for *Los Angeles Times*.
had big-city papers and small
s. We shared a need. But it was
rating trying to come together."

hile the wired world moved at warp
l, New Century spent 18 months
g a permanent CEO and two years
ing an electronic doorway to 140
papers. By the time it became wired
une, not only was Microsoft ahead
its Sidewalk.com online city guides,
New Century's own partners also
launched competing ventures. "This
is really racing," says Al Sikes,
former Federal Communications
Commissioner who is president of Hearst
Media. "Organizations of a number
equals can't turn on a dime."

ke nine parents with a new baby,
couldn't even choose a name.
e wanted news. Others wanted
ifieds. Tribune Co. was so exas-

MAN BITES BOARD Partners battled so bitterly that they wound up pursuing their goals on their own, outside the new business

perated, it joined America Online Inc.
in a classified service, becoming a New
Century pariah.

The most divisive issue was a pro-
posal by Winter to bring in as a partner
Kleiner Perkins Caufield & Byers, a
San Francisco venture capitalist, that
could also take the venture public. The
vote was split between those compa-
nies dominated by newspapers and
those more multimedia-oriented. Cox,
Tribune, and Hearst favored the idea.
Gannett was neutral. Knight-Ridder,
Washington Post, New York Times, and
Times Mirror argued that New Century
should push all its profits out to affil-
iates. The debate dragged on for months,
ending on a sweltering summer day in
1996 in a hotel room a half-mile from
Knight-Ridder's *Miami Herald*. The
proposal was defeated 5 to 4. "The fall-
out from that plagued New Century
going forward," says Bob Ingle, presi-

dent of Knight-Ridder New Media.

In June, New Century hired de Boer,
44, a former Home Box Office executive
who had been running his own media
consulting firm. He pulled together top-
rate executives and veteran journalists.
But, by all accounts, he was a poor com-
municator. When board members flew
to New York, where they wearily lo-
cated New Century for de Boer's con-
venience, they got no updates, no ma-
terials. "We turned the business over
to him to concentrate on ours," recalls
Ingle. "We should have given him more
guidance."

COLD BUTTON. But they were busy do-
ing other things. Knight-Ridder was
creating Real Cities to link 32 newspa-
per Web sites and run classifieds for
jobs, cars, and real estate. Tribune,
Times Mirror, and Washington Post
were building an online advertising net-
work called Classified Ventures. Tribune
also poured \$20 million into AOL's Digital
City online guides. Cox was developing
AutoConnect classified service and is
now in discussions with Microsoft to
link with Sidewalk.com, say industry
sources. Winter says simply: "We're
talking to a lot of people."

The board was paying little attention
when de Boer hatched his first major
plan: NewsWorks.
Run by former
Sports Illustrated
Managing Editor
John Papanek, it
posted stories daily
and linked to 140
sites. But small pa-
pers said they were
neglected, and big
ones feared it would

steal eyeballs. "We didn't need it, and it
was competitive," says the *Los Angeles*
Times' Chandler. So many papers buried
the NewsWorks button on their home
pages, leaving the site with little traffic
and few advertisers. Last year, adverti-
sers spent \$500 million on the Internet—
only \$1 million of it at New Century.

The partners ultimately invested
more than \$25 million in the virtual ven-
ture. But late last year, New York
Times refused to pay another penny.
Papanek left to launch *ESPN Magazine*
and de Boer began a fruitless search
for a high-tech partner. In February,
they shut down NewsWorks and laid
off half of its 70 employees. De Boer
asked for funding to reshape New Cen-
tury into an advertising shop. The board
decided instead to pull the plug, coming
to a remarkably quick agreement—for
the first and final time.

By I. Jeanne Dugan in New York

THE THREE MARKETEERS

Can these trade warriors rescue Clinton's initiatives?

Richard W. Fisher outperformed the market two-to-one when he managed a \$170 million hedge fund in Dallas. His forte: finding failing companies and then helping to turn them around. "I'm a distress guy, going into situations others view as hopeless," he explains.

Nowadays Fisher's business cards read Deputy U.S. Trade Representative—and the parallels couldn't be more striking. Once again, he's trying to reverse the fortunes of a troubled enterprise: the Clinton trade agenda. Fisher, 48, is one of "the Carter Kids"—three Washington veterans of the 1970s on a mission to salvage trade policy, underwater since the death of fast-track trade legislation last fall. The others are David Aaron, 58, new Commerce Under Secretary for international trade, and Stuart E. Eizenstat, 55, Under Secretary of State for economics, business, and agricultural affairs.

With U.S. trade-liberalization initia-

tives floundering in Asia, Europe, and South America, the new team has no lack of challenges (table). On Capitol Hill, the Administration must work to reassemble a 50-year congressional consensus for free trade that disintegrated with Clinton's failure to win fast-track negotiating authority. So when the three aren't flying off to world capitals, they will be wearing out the chairs in congressional hearing rooms, explaining why the U.S., now so dependent on exports, must push for freer markets at home and abroad.

"CRITICAL MASS." Foreign leaders will be an even tougher sell. But the Carter Kids have a strategy: Persuade a "critical mass" of countries to voluntarily liberalize in one market sector—as was done in 1996 and 1997 with multilateral agreements on information technology and financial services. Talks are now aimed at environmental services, chemicals, medical equipment, fish, toys, and jewelry, among others. And many deals

can be cut without congressional approval since they won't affect U.S. law.

Groups of nations will also be enlisted to pressure recalcitrant governments to free up their markets. That's the current game plan being used against Japan, which is under joint attack by Europe, Canada, and the U.S. to open its doors wider and stimulate its economy. "Leadership today means rallying others to our cause," says Eizenstat.

The first big test of the team's powers of persuasion comes on Apr. 1, when Clinton travels to Santiago, Chile to begin talks on the Free Trade Area in the Americas (FTAA), his plan for a tariff-free zone embracing the entire Western Hemisphere. Latin American see Congress' fast-track vote as a repudiation of further trade deals. "The leadership in South America is deeply disappointed—devastated, really, over the loss of fast track," says Richard E. Feinberg, a University of California at San Diego expert on Latin America.

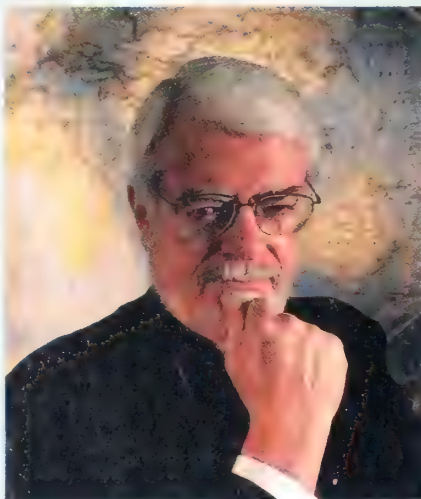
Failure of the FTAA would be a win for Brazil: South America's largest economy fears a free-trade area dominated by the U.S. and has urged a go-slow approach. With no FTAA, Brazil could negotiate smaller, South American free trade zones that exclude the U.S. The Carter Kids' plan: Convince the Latin Americans in preliminary talks in Costa Rica on Mar. 18-20 that Clinton will give fast track in time for FTAA approval by 2005. If they fail, Clinton's Santiago trip may prove to be the biggest trade embarrassment of his tenure.

'CARTER KIDS'



RICHARD FISHER

Deputy U.S.
Trade Representative



DAVID AARON

Under Secretary of Commerce
for International Trade



STUART EIZENSTAT

Under Secretary of State for Economic,
Business, and Agricultural Affairs

The clock is also ticking on China, desperately wants Washington to give its membership in the World Organization. The U.S. business thinks that dropping opposition to China's membership will induce Beijing to buy American. And China's core supporters are weary of the battle in Congress for Most Favored Nation trading status. But following WTO membership, the Administration wants a promise from China to lower barriers to imports, to end subsidies to favored industries, to dismantle state-owned enterprises, to employ 100 million workers. Clinton would invite China to join the WTO and give it a warm welcome in the White House. If, as tentatively planned, he travels to China this fall. The Administration wants to reward China for not devaluing its currency. Devaluation would hurt the U.S. trade deficit. That puts the trade trio and their bosses, U.S. Representative Charlene Barshefsky and Commerce Secretary William M. Daley, on the hot seat. They will have to make the best possible terms from the start. Yes, admits Aaron, Chinese officials "have shown a great deal of re-

AN AGENDA IN TATTERS

FAST TRACK Failure to secure "fast-track" trade legislation from Congress means that Clinton will be heading to Chile in April to kick off negotiations for an all-hemisphere free-trade deal with a weakened hand.

CHINA Washington has been negotiating with China over the terms of its entry into the World Trade Organization. But Beijing is resisting opening its markets to imports and it wants a delay in ending subsidies to millions of state-supported business enterprises. Clinton will be visiting China in late 1998.

JAPAN Administration efforts to pressure Japan into stimulating its

economy so it can buy more imports from the U.S. and from struggling Asian nations are stalled. Tokyo is also refusing to open its markets further and to help U.S. car companies sell in Japan.

IMF The White House wants \$18 billion in additional funding from Congress for the IMF. But Congress is skeptical because of the mixed success of the IMF bailout in Asia.

INVESTMENT Negotiations in Paris to unite the 28 countries of the OECD in a treaty covering \$315 billion in annual foreign investment flows have broken down.

DATA BUSINESS WEEK

sponsibility in not devaluing, and they deserve credit for it...but we are not going to suddenly cave in."

Rescuing Clinton's trade agenda will require more than persistence in Congress and diplomacy abroad, however. The members of the new trade troika will also have to keep their often-warring

bureaucracies in check. The three agencies "have always viewed each other with some suspicion, but since the three of us know each other so well, that shouldn't be a problem," says Aaron. Maybe not, but the Carter Kids are about to test the depth of their friendship.

By Paul Magnusson in Washington

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FAST EDDIE'S FUTURE BANK

How Crutchfield is racing to revolutionize First Union

In 1951, Katherine S. Crutchfield took her son, Eddie, to the First National Bank of Albemarle, in the town of Albemarle, N.C., pop. 11,800. Escaping from the sticky heat of the Tarheel summer, the 10-year-old loved the feel of the cold marble floor on his bare feet. His mother, a teacher who had studied economics at The Women's College of North Carolina in Greensboro, whispered in his ear: "You might want to think about banking as a career." Young Edward E. Crutchfield Jr. quickly assessed the prospects. A gray-headed man he recognized, Hazel Morrow, carefully counted currency, standing erect behind a desk, separated from the people of Albemarle by thick, black steel bars. Through a chest-high hole in his cage, Morrow doled out cash, circulating it to the free civilians.

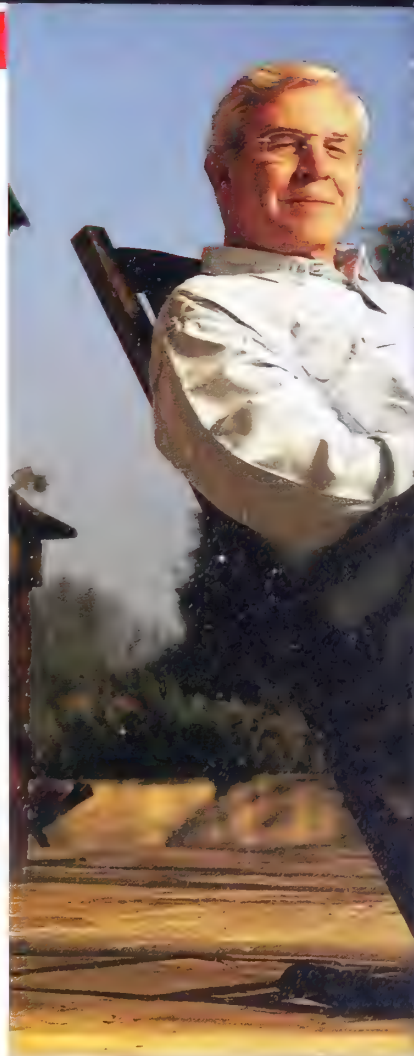
His mother's vision horrified the young Crutchfield. "It was tantamount to saying you might as well think about a career in jail—spend your life behind bars," Crutchfield recalls.

Crutchfield did become a banker, but in his 33-year career at First Union Corp. he has knocked down the bars of banking with a vengeance. Beginning in the mid-1980s, he took Charlotte's third-largest bank on an acquisition spree—more than 70 deals in 10 years—that transformed it into the sixth-largest bank in the U.S., with \$206 billion in assets. Along the way, he tested conventional banking customs and regulation.

Now, with his initial banking acquisition goals mostly accomplished, Crutchfield is focusing on the biggest bar-breaker yet: a top-to-bottom redesign of the entire retail operation of one of the country's largest banks. Crutchfield calls his concept Future Bank. It's a mix of all the elements he believes will be necessary for banks to survive onslaughts from brokerage firms and mutual-fund houses and from industry consolidation and technology. He is developing an aggressive, sales-oriented culture at First Union, unleashing a commission-only sales force to cold-call middle-market customers. He's building First Union's presence in product lines such as mutual funds and insurance.

"FUNDAMENTAL CHANGE." He's also reaching customers through an array of new channels: everything from Internet banking to minibranches to a new call center two-thirds the size of the Pentagon. On Mar. 4, he snapped up The Money Store Inc., a huge and highly profitable consumer credit company and among the savviest players in the subprime market, for \$2.1 billion. Overnight, the deal turned First Union into the nation's largest home-equity and small-business lender and No. 3 in student-loans.

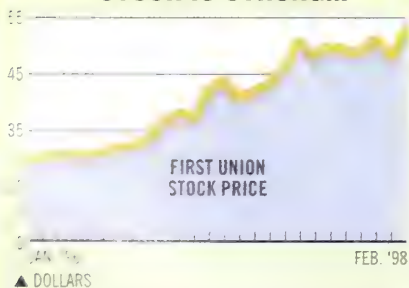
To capitalize on these channels, Crutchfield has built one of the industry's largest data warehouses. He is mining the raw data to custom-fit sales pitches to individual customers. To make sure it all comes together, he has put



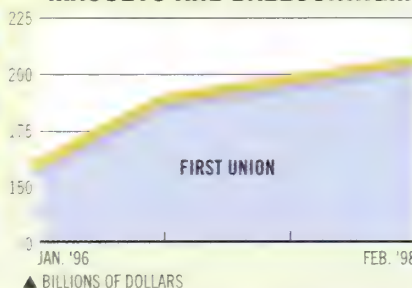
First Union on an expedited timetable demanding that the Future Bank concept roll out from its Atlanta test market into companywide implementation by the end of 1998. "This is massive," says John R. Georgius, First Union president and Crutchfield's closest strategy adviser. "This is a huge, fundamental change to what we do."

Analysts applaud Crutchfield's ambitions, though some are skeptical that he will see a big payoff soon. The bank stock has soared 151% since January 1995. First Union's return on assets and

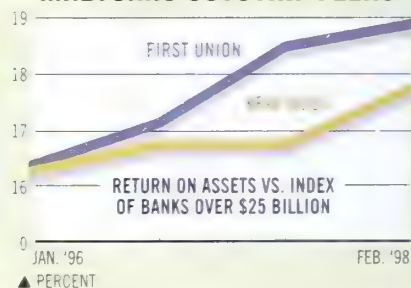
STOCK IS STRONG...



...ASSETS ARE BALLOONING...



...RETURNS OUTSTRIP PEERS



DATA: BLOOMBERG FINANCIAL MARKETS; KEEFE, BRUYETTE & WOODS INC.; FIRST UNION CORP.



have outstripped the Keefe, Fite & Woods index of 50 major Assets have climbed from \$159.6 in 1994 to \$205.7 billion in 1997. Crutchfield is rewarded handsomely. His five-laden compensation package rose \$19.5 million last year. Banks like Citicorp and Norwest Corp. have experimented with redesigns, and others like National Bank Corp. and Huntington Bancshares Inc. have made significant investments in data warehouses, none as many pieces, and none on a systemwide rollout. Crutchfield's buying spree, combined with his Bank investment, contributed to a rise in net income last year. He expects per-share income to climb 14% for the next two years. "They're where they need to be," says Merrill Lynch & Co. analyst Sandra J. Flannery. But, she adds, "they're further along than almost any other bank." Scott D. Nelson, research director at Partner Group Inc. in Stamford, Conn., says: "First Union is doing the consistent job across the whole spectrum of new banking systems."

The focus on an internal revolution is a big change for a man who has spent most of his career turning heads with his insatiable appetite for buying banks. At one point, he was scooping up a bank a month, often paying eye-popping prices—amply justifying his sobriquet "Fast Eddie." Last summer, Crutchfield described the style he used in talks with Signet Banking CEO Malcolm S. McDonald, which First Union bought for \$3.3 billion: "I had a stack of \$1 billion bills and just laid them out for him one by one until he said yes."

Unlike rival Hugh L. McColl Jr., CEO of NationsBank, whose deals have taken him as far afield as California, Missouri, and Texas, Crutchfield has built his powerful franchise exclusively along the Eastern Seaboard—the golden crescent of U.S. banking, from primarily coastal states running from Connecticut to

Florida. Among the last pieces of this mosaic was Philadelphia-based Core States Financial Corp., which First Union bought in November for \$16.5 billion, history's largest bank merger.

FOLKSY VENEER. Crutchfield has mastered the Southern art of concealing his competitive blood lust behind a veneer of folksy witticisms. He regales people with deal stories as if boasting about the big ones he bagged on his latest fly-fishing forays to Montana or New Zealand. But in more reflective moments, he confesses that his most important deal decision was listening to Georgius in 1985 when he suggested putting every acquired bank on a single, unified computer system that would operate throughout the First Union franchise. That strategic call helped make Crutchfield's acquisition rampage possible, and now allows his rapid transformation of First Union's retail strategy.

Having a single system has enabled Crutchfield to outbid competitors on deals because it helps him integrate ac-

quired banks into First Union in just nine months—easily twice as fast as any competitor. It has limited First Union's Year 2000 costs to just \$55 million, compared with Citicorp's industry record \$600 million estimate. And with the system's backbone becoming such a crucial part of the redesign of retail practices, the single system is proving its worth again.

Crutchfield is an unlikely man to lead a systems-intensive transformation of one of the nation's biggest banks. By nature, he's more Lud-

dite than leading-edge. Any department at First Union wishing to install voice mail still must win his personal approval. His home computer is rarely used; and there's no PC in his spacious office. While he grudgingly invests in the bank's push into Internet banking, he confides to associates that he doubts any bank will make real money from the Internet anytime soon.

Crutchfield has always lived life in his own style. A high school football star, he and a friend once sent two Marines to the hospital after a fight at a drive-in movie. He turned down a schol-

EDWARD E. CRUTCHFIELD

BORN 1941 in Detroit; raised in Albemarle, N.C.

EDUCATION Attended Davidson College on a football scholarship. MBA from Wharton School, 1965.

WORK EXPERIENCE Joined First Union in 1965; president in '73, CEO in '84.

ACHIEVEMENTS Acquisition spree led to nickname "Fast Eddie." Acquired more than 70 banks in 10 years, and built First Union into nation's sixth-largest.

PERSONAL An avid fly fisherman; on Mar. 6, inked \$2.1 billion purchase of the Money Store while on fishing trip in New Zealand. Dislikes small talk. Technological Luddite—he doesn't have an office PC—but his bank is a tech leader.

DATA: BUSINESS WEEK

arship offer from the University of North Carolina and instead went to Davidson College near Charlotte for its academic challenges. His mother's entreaties paid off, and rather than becoming a lawyer and judge like his father, he matriculated at the University of Pennsylvania's Wharton School.

As graduation approached, Crutchfield interviewed at each of Charlotte's three big banks—NationsBank's predecessor, North Carolina National Bank, Wachovia, and First Union. Secretly coveting the top job at whatever bank he chose, the 23-year-old asked to spend an extra day at each bank, so he could prowl the halls and furtively size up the people he would be competing with. He decided First Union had the most deadwood, and he took that job. His \$7,200 initial salary was both the lowest of his offers and the smallest wage of anyone in his Wharton graduating class.

IMPECCABLE TIMING. His instincts and timing proved impeccable. The man who hired him, Clifford Cameron, was on his way to seizing control of the bank. Almost from the start, Cameron began grooming Crutchfield as his successor. To improve Crutchfield's management style, Cameron assigned him to revamp the personnel department after noticing a shortcoming: Crutchfield was hell on people. "He couldn't understand why people couldn't get things done," Cameron recalls. Crutchfield could also never understand why anyone would want to leave First Union and profanely chewed out people with talent who resigned. He saw no value to outside activities, such as charity functions. Still, he shaped up, and was astounded when Cameron named him president of First Union Bank at just 32.

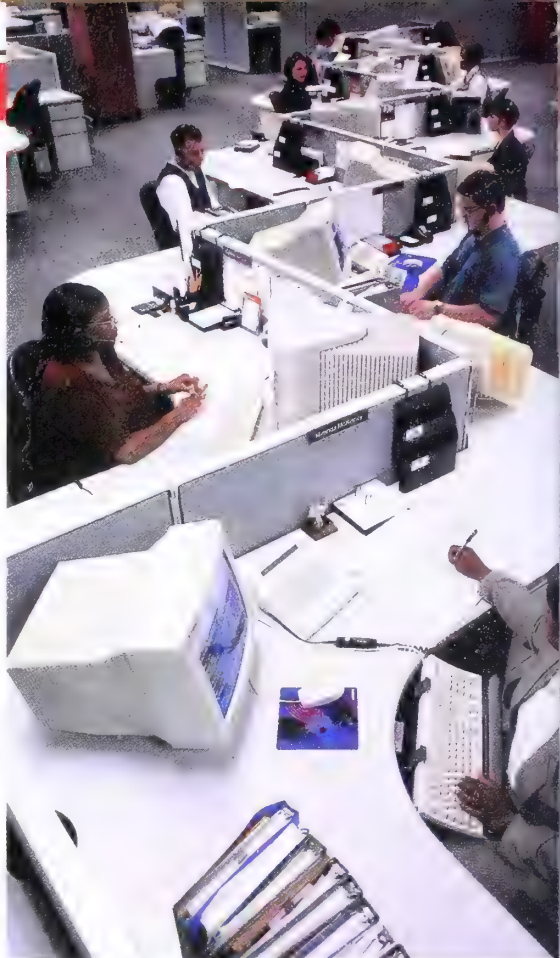
The job he is taking on now—re-designing First Union's retail operations—is no less daunting. The genesis of Future Bank was four years ago, at a meeting of First Union's top executives at the Greenbrier resort in White Sulphur Springs, W. Va. Crutchfield and Georgius said they were tired of seeing brokerage firms and mutual-fund companies snare the bulk of their customers' assets. "We're delivering the same products we delivered 30 to 40 years ago, with the same old-fashioned delivery system," Georgius recalls saying. "We have to change, or we'll just continue to lose share."

Now, Future Bank is rolling out

HARD SELL: Sales from huge centers like this one near Charlotte are key

across the entire First Union system. To make Future Bank work, Crutchfield and Georgius assembled a number of parts that were missing from First Union's portfolio four years ago. In 1985, they introduced the capital management account, dubbed CAP. It gives customers an attractive return on their funds by unifying brokerage and banking activity and sweeping free cash into a bank certificate of deposit or mutual fund, similar to Merrill Lynch's cash management account. Crutchfield paid \$143 million to buy the Evergreen mutual funds, giving First Union a foothold in the fast-growing fund business. He recruited a star of the credit-card industry, Jack M. Antonini, to mine the bank's database of customer information for profitable new marketing schemes. And in 1997, First Union completed construction of its center for customer-service calls outside Charlotte. At Crutchfield's insistence, the 160-acre site is nearly triple the size of the plot Georgius first proposed, allowing room for major expansion.

The overriding notion of Future Bank is to integrate the back-office improvements such as the call center, CAP account, fund offerings, and sophisticated marketing into the action end of the bank: the branch. Crutchfield arranged



the branches so that customers entering the building are met by greeters, whose job is to find their needs and, if possible, direct them away from tellers and lending officers and toward automated teller machines (ATMs), or connect them by telephone to the call center. Interception by a greeter saves money: ATMs handle transactions for 27¢ apiece, while tellers are slower and more costly, at \$1.25 a transaction. Each branch receives several hundred names every day from a computerized system that identifies the most attractive prospects and suggests what products to sell them.

To boost sales, Crutchfield changed the compensation structure, putting everyone in the branches, from tellers to branch managers, on an incentive system based heavily on sales increase. He created job descriptions and invited all employees to select the job they were most suited for. First Union recruited heavily outside the industry, to attract former stockbrokers and consumer-product salespeople with more knowledge of selling than of old-style banking. "There will be a fair number of people who decide they do not want to sell," Georgius told First Union managers at a recent Future Bank orientation session. "If they don't want to see they need to go find something they feel comfortable doing, but our company has got to move on." The rollout move



GOOD CALL: President John Georgius suggested in 1985 the bank unify its computer system

FUTURE BANK

Crutchfield is trying to revolutionize retail banking

LL, SELL Hiring nonbankers, giving incentive-based compensation, redefining jobs is part of a new "sales culture."

PHONES A huge new call center outside Charlotte enables First Union to make 12,000 sales calls and 7,000 service calls each day.

CD MARKETING Mining huge data warehouse, First Union wants to customize its marketing efforts on a one-on-one basis.

REDESIGNS Greeters at the branch take customers to ATMs or telephones away from labor-intensive loan officers to make loans.

IN THE BASE Crutchfield paid \$1 million for the Money Store, a franchise firm, to broaden his product line and his customer base.

DATA: BUSINESS WEEK

...st that Crutchfield and Georgius ... people to bid on new jobs before ... compensation structure was com- ...—and got plenty of takers, thanks ... promise of incentive-based pay.

TRY HAM. The new plan will shift incentives to salespeople, not their managers, and will reduce payouts to top performers while boosting bonuses for others. It boosts incentives to 10% of total compensation for all sales staff over the next two years. An employee who produces \$100,000 in monthly revenue for the bank will receive \$2,850 in monthly incentive pay, up from \$236 under the old plan, while one who produces just \$50,000 would see incentive pay drop from \$326 to nothing. "When I came to First Union they gave you a country ham and a turkey at Christmas if you had a turkey," Crutchfield told a group of executives meeting to approve the plan. "Now, we're paying them out in cash on the barrelhead."

...key to Future Bank is people like ... ara Binko-O'Connor. She has an of- ... at a First Union branch in Cobb ... ty, Ga., but her real work space is ... Accura Integra. Working from a ... book computer, she scans names ... prepares presentations as she drives ... offices and homes around Atlanta. ... books appointments on her cell ... e. Banks always have used calling

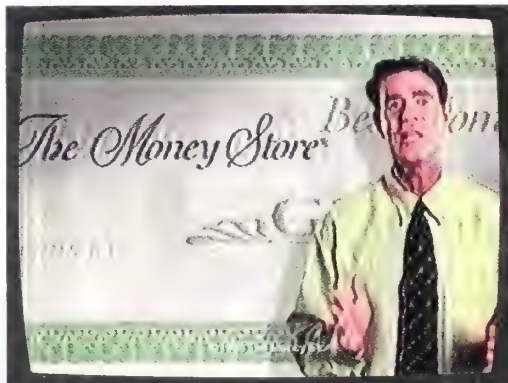
officers to visit silk-stocking clients. But Binko-O'Connor's quarry is further down the economic scale: people with about \$75,000 in annual income whom she can persuade to consolidate all their financial affairs at First Union. "We're looking for people who are going to be affluent rather than people who are affluent," she says. When she can, she turns new customers over to a service representative who does actual banking tasks, freeing her to hunt for new money.

Binko-O'Connor draws no salary and is paid purely on commission, with no limit to the amount she can earn. In one morning, she visits a lawyer whom she has known a long time to introduce his new service representative and to prod him for referrals to some new prospects. Between appointments, she scans a list of plastic surgeons in an office building where she plans some cold-calling visits. She meets with a health-care executive who is a longtime client, and in talking shop discovers that his business could use help from First Union's equipment-leasing unit. Binko-O'Connor's eyes sparkle with the prospect: She gets a take for 12 months on any new business she brings to the bank.

Deal-closing initiative like Binko-O'Connor's is just what Crutchfield expects from the Future Bank, and he has designed it into the systems at the call centers, too. By the end of 1999, Crutchfield wants 40% of First Union's product sales to come from the call centers, up from only 30% today in the Atlanta experiment. The center bombards

persuade a customer to move a \$300,000 CD from Barnett Bank to First Union. "You know they're being taken over by NationsBank," he says. "If you're not satisfied, which I don't think you will be, with what they're trying to put you in, then I'm sure we'll be able to do better for you here."

Competitors and analysts are eyeing the Future Bank rally with a mix of curiosity and skepticism. John L. Brennan, head of channel strategy and development at NationsBank, notes that the nation's third-largest bank won't easily be trumped by its crosstown rival. NationsBank is getting good results from its supermarket branches, an outlet First Union has ignored, and is converting them into full-service operations. It's ahead of First Union in PC banking. And it's introducing a money management account to match up with First Union's CAP. "We really don't see any activity that would come from our competitors to do anything that would cause our customers to move from NationsBank to anywhere else," says Brennan.



The \$2.1 billion Money Store deal turned First Union into the nation's largest home-equity, student-loan, and small-business lender

MONEY STORE SPOKESMAN JIM PALMER

the senses with exhortations to sell. A banner on the wall reads "Keep Florida Green"—a reference to First Union's corporate color and the tag line for the bank's effort to thwart NationsBank's efforts to dominate Florida following its acquisition of Barnett Banks Inc. last year. Photocopied certificates recognizing outstanding sales and service efforts paper walls and cubicles. Ceiling video displays show how many calls are answered, average hang-up rate, and incoming volume. At one phone, sales representative Doug Freas is trying to

Crutchfield acknowledges rivals, but he doesn't worry much about them. He plans to spend half his time this year in employee meetings, fielding questions in a town-hall format, and introducing them to the new First Union sales culture. And he's accelerating his Future Bank campaign. He may not wind up precisely where he thinks he will. But with the headstart he's got on modernizing the face of retail banking, Fast Eddie is likely to get there before anyone else.

By David Greising in Charlotte, N.C.

COMMENTARY

By Dean Foust

STUDENT LOANS DON'T NEED CLINTON'S TINKERING

Over the next few weeks, millions of high school seniors will find good news waiting in their mailboxes, as colleges begin sending out acceptance letters to next year's eager crop of freshmen. But if the Clinton Administration continues to play politics with the government's student loan program, some of those same students could be in for a rude shock when they arrive on campus next fall—and discover there's not enough financial aid to cover their tuition costs.

This unpleasant surprise could be the result of the Administration's hardball tactics with the 5,000 or so banks that make \$25 billion in student loans each year at Uncle Sam's behest. At issue is a change, effective July 1, in the arcane formula that determines the interest rate banks can charge. The old formula guarantees the banks 3.1 percentage points above the recent average for 91-day Treasury bills. The new formula will pay banks one point over the rate for 10-year Treasuries.

BIG DROP. But the unexpected drop in long-term rates has created a potentially major problem: Lenders complain that the plunge in what they earn—from well above 8%, now to 7% or less—could render much of their student lending marginally profitable. "They're expecting banks to make these loans at 40%-50% less than they can lend elsewhere," complains J. Paul Carey, executive vice-president for marketing at Student Loan Marketing Assn. "I don't think banks are going to put out \$25 billion as a loss leader each year."

So far, White House officials are showing little sympathy to the banks' plight—preferring to play up the potential savings to students: Vice President Gore boasts that the new formula would save the average graduate with \$12,000 in loans, roughly \$650 over 10 years. If the Adminis-

tration's lowball offer is simply a ploy to determine how much of a cut banks will accept, that's fine. But it's possible that, despite its claims to the contrary, the White House has an ulterior motive: To cut rates so low that many banks will simply exit student lending, leaving schools with no choice but to steer some students into the Education Dept.'s four-year-old direct-



lending program—which they have been loath to do.

Despite the Administration's bold predictions that it would by now be making the bulk of all student loans, its share of all new loans is at 32%—a far cry from the 40% it briefly claimed two years ago. And those vaunted savings the Administration promised once the banks were cut

out? Sure, accounting gimmickry makes direct lending look to be less expensive, "but when you include the administrative costs, the programs are comparable," notes an official at the Congressional Budget Office.

If its goal is to drive out the banks, the Administration should be careful what it wishes for. If too many banks flee the pro-

gram this summer, thousands of would-be scholars could find themselves scrambling to secure a student loan this fall. That's because, as banks privately warn, they'll cherry-pick the most profitable loans—the \$50,000 debts of graduates of Harvard University and other elite schools—while shunning unprofitable \$5,000 loans, which largely go to students at trade schools and community colleges. Jerry Steele, executive vice-president of a

California state-run student aid program, frets that banks will pull out of schools "that are higher risk because of their default rate or eliminate institutions with whom they do not have an ongoing relationship."

HOLDING THE BAG? Over the long term, the government's sorry record of managing lending programs doesn't leave even Democratic lawmakers confident that the Education Dept. will be up to the task of collecting on the billions in direct loans when they come due. The Education Dept., indeed, will likely be stuck with the lowest quality loans. "The Federal Housing Administration, Veterans Administration—our experiences with large-scale government lending hasn't always been good," notes Representative Paul E. Kanjorski (D-Pa.).

"Bankers are closer to the market and better able to prevent fraud and abuse from creeping into the system."

In promoting the direct-lending program, Clinton officials have repeatedly vilified bankers for reaping lush profits at the expense of student borrowers. But time has shown that the student loan program works pretty well just as it is. If bankers are enjoying windfall profits, it's largely due to efficiencies in marketing and collecting student loans. But it may be time for banks to share some of those savings with taxpayers—by accepting a quarter or half-point interest rate cut. And perhaps it's time for the inveterate tinkerers at the White House to resist the urge to fix something that isn't broken.

Foust covers finance from Washington.

Washington's
hardball tactics
with banks may
end up hurting
the poorest
students

CONGRESS HAS MADE IT *more*
attractive THAN EVER
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New tax legislation offers investors some of the greatest retirement benefits since Social Security was introduced over 60 years ago. Traditional IRAs have become more flexible, and the new Roth IRA, available now for tax year 1998, makes it possible to invest on a tax-free basis. Confused? You needn't worry: Charles Schwab is here to help provide the answers you need to move confidently ahead.

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For immediate help, visit the IRA ANALYZER at www.schwab.com

Charles Schwab

TAKEOVER BATTLES

HEAVYWEIGHT WRESTLING OVER A FLYWEIGHT INSURER

That thump may be Hank Greenberg tossing Henry Silverman

Maurice "Hank" Greenberg, the tough-minded CEO of American International Group, the world's largest insurance company, usually gets what he wants. But then, so does Henry R. Silverman, the fast-moving CEO of Cendant Corp. The two seasoned deal-makers have been enmeshed for weeks in a bidding war over American Bankers Insurance Group, a little-known but alluring Miami-based credit insurer. Right now, the bids are matched. But AIG is the favored bidder. Arbs say that Silverman will have to significantly up the ante to win the prize.

For one thing, it has the backing of American Bankers, who approached AIG. It's a much better-known player: Cendant was created only last December, a combination of HFS Inc., a travel and real estate giant, and CUC International Inc., a direct marketer of discount buying clubs. And the fit is better: AIG has the broad international presence American Bankers covets.

Silverman could still win. "This will all be decided on who can make a higher offer," he says. "If we have to bump [our offer up], we have to do it by the end of March"—when shareholders will vote on the AIG offer.

WARY INVESTORS. How much higher is the question. Despite Silverman's stunning track record in creating shareholder value from a melange of brand names from Avis to Century 21, some of American Bankers' investors, and its top management, are wary of the new company. "The board couldn't take a position on Cendant because the company was only six weeks old," says American Bankers CEO Gerald N. Gaston. "It's like looking in a mirror and saying, 'This guy's going to be a great football player.' He might be, but you don't know." Says one institutional investor, "Bumping it up a little is not going to win. I personally believe

AIG can better manage the future of American Bankers than Cendant. I think it's a better fit with AIG."

To match Cendant's bid, AIG was forced to pay \$58 a share, or \$2.7 billion. Some arbs and analysts say Cendant would have to come back with \$60 a



GREENBERG



SILVERMAN

THE PRIZE

Gerald Gaston's American Bankers, which makes big bucks insuring loan payments

share to overcome bias in favor of AIG. Others say a counteroffer could go as high as \$64, depending on how badly Silverman wants American Bankers. "At 58, it's already past the value of American Bankers on its own—we're now talking the belief of both AIG and Cendant that they will add additional value

to the merger," says one arbitrageur.

Until now, American Bankers has gotten press mostly on its employee amenities, such as the day-care center and school on its grounds, as well as the swift rebuilding of its headquarters after Hurricane Andrew in 1992. So why all this interest in a little-known company? Quite simply because American Bankers is by far the largest player in credit insurance, which pays off balances in the event of job loss, disability or death. It leads the industry in third-party direct marketing and is among the top insurance direct marketers.

Cendant and AIG have somewhat different aims in going after American Bankers. AIG wants access to new channels of distribution and product lines. Silverman wants new products to sell through his direct-market operations. He sees scale benefits in combining the two companies and wants to push American Bankers' products using Cendant's ties with credit unions and community banks.

But American Bankers may not be quite the prize it seems. Very much a niche player, it has moved in and out of markets over the years as competition intensified. It has been finding it increasingly difficult to cultivate new markets domestically.

While it has posted strong revenue and net-income gains over the past five years at compound annual rates of 17.1% and 22.3% respectively, internal projections contained in the Jan. 30 proxy statement show those figures falling to 14.4% and 16.2% through 2001.

That was why American Bankers in May began discussions with AIG. Its main potential is overseas. But the process of expanding overseas has been slowed by the need to obtain foreign regulatory approvals and local partners, executive say, and AIG's global reach would bypass those hurdles.

American Bankers employees seem to be taking the battle in stride and are watching their holdings increase in value. "I like to see it going up," says Elroy Allen, a maintenance manager for 1 years who owns 2,000 shares. If Henry Silverman blinks and decides to up the ante, shareholders like Allen will have even more to smile about.

By Gail DeGeorge in Miami, with Amy Barrett in Philadelphia and Susan Jackson in New Haven

GENE G. MARCIAL

OUT OF THE FIRE AT NATIONAL STEEL

At first glance, it's easy to see why investors have for the most part turned away from National Steel, which hardly budged in this bull market.

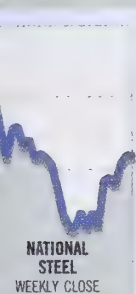
Securities & Exchange Commission has been looking into its books following allegations of accounting manipulation.

And the Asian fallout has added to investor concern about earnings at National, which is 51% owned by NKK of Japan. But a second look has prompted some big players to buy into this fourth-largest U.S. integrated steel company. Here's the scoop.

These pros argue that National Steel has done a lot to turn itself around. The company slashed total debt in 1997 from \$781 million to \$93 million. It has started to pay a 7¢ quarterly stock dividend. "Several positive changes are going on at National that aren't yet widely known," says one New York investment manager who has been accumulating shares. He backs the SEC probe—which was prompted by National's own audit committee's restatement of earnings—will conclude in the next few months. He says the company has gotten no indication that the agency has found anything amiss. In fact, the audit that the company undertook sought to check allegations from critics of a lack of controls and improper allocation of cash reserves.

This money manager believes that once the SEC ends its inquiry, "National Steel could well be a takeover target of a larger steel company." He speculates that given the right offer, NKK might decide to "cash in its chips and pursue its interest." When National made its secondary public offering of 6 million shares in January, 1995, at 16 a share, NKK sold some shares, reducing its ownership to 51% and its voting power to 37.6%.

FORGING TURNAROUND?



SEP. 17, '97 MAR. 11, '98
DOLLARS

DATA: BLOOMBERG FINANCIAL MARKETS

Michael Gambardella of J.P. Morgan Securities says that National will likely buy back 10 million shares, or 23% of outstanding shares—nearly half its public float. The company has a cash hoard of \$338 million, or \$8 a share, he notes. Gambardella figures it will earn \$2.40 a share this year and \$2.75 next year. At 16 a share, the stock is undervalued in a group that is rebounding, say some pros.

WHAT'S IN A NAME ON THE NET?

On fire. That's what Internet stocks have been. One that's not yet widely known and not yet too visible—and making money: Network Solutions (NSOL), whose stock has zoomed from 12 a share in late December to nearly 24 on Mar. 11. It's the leading provider of Internet "domain" registration services worldwide. In other words, Network Solutions is the exclusive registrar—empowered by its agreement with the National Science Foundation—for all "top-level" .com domain names as well as the "second-level" names that are within the .net, .org, and .edu categories.

"The .com top-level domain represents more than 90% of the company's registrations," says James Pettit of Hambrecht & Quist. So Network Solutions "is at the core of the Internet, creating unique addresses from which to communicate and conduct commerce," explains Pettit. Although the government may open the field to competitors next year, he believes that "Network Solutions will remain the key player in the domain-name space business."

The customer pays a two-year registration fee of \$100 to Network Solutions and \$50 annually thereafter. The company has signed pacts with 40 Internet access providers, including MCI, AOL/PrimeHost, UUNet, Sprint, and GTE (BBN). The company also signed strategic marketing pacts with such companies as Dun & Bradstreet, Microsoft, and

KING OF ITS DOMAIN



SEP. 17, '97 MAR. 11, '98
DOLLARS

DATA: BLOOMBERG FINANCIAL MARKETS

Verisign. Pettit figures Network Solutions, which has \$5 a share in cash, or \$80 million, will earn 51¢ on revenues of \$72.7 million in 1998, and 85¢ on sales of \$110.6 million.

HOW U.S. SURGICAL IS HEALING

Once a glamour stock that soared as high as 131 a share in early 1992, U.S. Surgical (USS) has come back to earth since and currently trades at 34. Analysts aren't thrilled anymore by this maker of laparoscopic products, surgical sutures and staplers, and ultrasound devices. Profit disappointments, caused mainly by pricing pressure and growing competition from larger rivals, have made buy ratings from the Street increasingly rare.

But lately the stock has displayed signs of renewed life, trading well above its 52-week low of 23 reached in early December. And some traders say the stock has shown upside momentum, with volume on several days hitting more than 1 million shares—or twice its average daily volume.

Why this new interest? A longtime watcher of U.S. Surgical thinks some pros are accumulating shares on the belief that either Abbott Laboratories or American Home Products is considering a move on the company.

"The story makes good sense," says a money manager who invests in medical-device and health-care stocks. "Both Abbott and AHP could use new medical products for the huge markets that they serve," he adds. And they can squeeze more efficiencies from U.S. Surgical's operations, especially in distributing products to hospitals worldwide. Revenues last year were \$1.2 billion. This money runner thinks U.S. Surgical is worth 50 in a buyout. Vivian Wohl of Merrill Lynch figures it will earn \$1.65 a share in 1998 and \$1.96 in 1999.

A spokesman says AHP is always looking for opportunities. But he wouldn't comment on U.S. Surgical, which also declined comment.

REJUVENATED STOCK PRICE



SEP. 26, '97 MAR. 11, '98
DOLLARS

DATA: BLOOMBERG FINANCIAL MARKETS

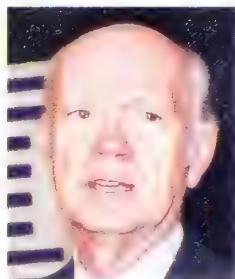
REPORT ON A
BUSINESS WEEK
EXECUTIVE
BRIEFING

presented in
association with

IBM

CONNECTIONS

COMPETITIVE STRATEGIES FOR THE AGE OF



"Corporations must prepare themselves for the eventuality of anything."

Regis McKenna
chairman, The McKenna
Group; author, *Real
Time: Preparing for
the Age of the Never
Satisfied Customer*

For many companies, the impact of the Internet has moved well beyond creating a simple "web presence" or developing an intranet. Instead, the arrival of e-business is rewriting the very fundamentals of business: redefining relationships with customers and suppliers, creating new business models, even redrawing the boundaries between industries. Myriad opportunities are being created for companies of every description. Because of these far-reaching implications, e-business is no longer something to be controlled by a marketing vice-president or the CIO. CEOs must handle the e-business initiative personally. That is why *Business Week*

and IBM created CONNECTIONS, a one-day, CEOs-only private meeting on the challenge, complexity, and evolving techniques of e-business. The meeting offered specific strategies for weaving the power of e-business into organizations.

e-business is still new, but there is a growing list of early adopters who are scoring big gains through their innovative use of the Internet for new go-to-market strategies, cost-saving back office solutions, and dramatic remakes of decades-old wholesaler relationships. These techniques, from leaders such as Charles Schwab & Co. and AMP, Inc., are the benchmarks of e-business today.

MAY ALL YOUR CHANNELS BE GOLDEN



Irving Wladawsky-Berger
general manager,
Internet division, IBM

"I'm convinced that the 'killer app' of the Internet is customer service leading to customer loyalty. When someone realizes that you are offering them personalized attention available anytime from anywhere, the channel to that customer becomes golden. And it will also be the least expensive way for you to reach that customer. The best way for the customer and the best way for you: It is the perfect combination and it is available now for companies of every size, everywhere.

"All the CEOs in this room and thousands of other business people around the world are in the process of building something wonderful. It doesn't have a name yet. It will combine the standards and connectivity of the Web with the substance, applications, and data of all our corporate information systems combined. And it will be truly universal. History shows that every time a new universal communications path has opened it has led to profound change in the way commerce is done. Clipper ships, railroads, telephones, broadcasting — and now the Internet:

The new universal connection quickly becomes more than a new channel. All of a sudden, the whole business community starts looking at every single business process, asking 'How can this new connection help me to improve that process?'"

BusinessWeek
EXECUTIVE BRIEFING

by Scott Shuster, moderator
*Connections: Competitive
Strategies for the Age of*



the Internet fundamentally changes the dy- namics of stock trading."

Elizabeth Sawi
executive vice-
president, electronic
brokerage enterprise,
Charles Schwab
& Co., Inc.

"Because it gives access to so much information, the Internet fundamentally changes the dynamics of stock purchasing," says **Elizabeth Sawi**, executive vice-president, electronic brokerage enterprise, Charles Schwab & Co., Inc. "People can research stocks in a way they never could before. So when we think about one-to-one marketing through the Internet at Schwab, we have to start by developing an understanding of that changed customer dynamic." And that is not an easy thing to do. **Regis McKenna**, one of the computer industry's venerable marketing gurus (he helped Intel in the very first computer chip) warned conference participants that "most of us are still doing business based on extrapolation of the past. Rather than thinking about radical, discontinuous change, we'll tend to look forward by looking backward. We won't do," says McKenna. "Corporations must re-examine themselves for the eventuality of anything." Some industries can do that, but others appear stuck in the analog past, unable to develop the mindset required. "Retailing is broken," says **Marshall Fisher**, co-director of the Fishman-McLendon Center at The Wharton School of the University of Pennsylvania. "Traditional retailing was designed for a time when there were a lot of customers but not enough to buy. The secret to success was supply. The new challenge is the consumer who has no time to shop. Traditional retailers are poorly equipped to cope with this, and yet there is a gold mine of unsatisfied customer need. The Internet e-business offer an excellent way for retailers to reach the best consumers."

Web of Challenges

To fulfill its potential, the Internet must create a new environment for business to live in. A creative process must occur simultaneously with a parallel process of destruction: The end, or at least the decline of traditional wholesaler relationships; the reshaping of entire industry structures. In the area of informational products, for example, many companies are faced with the bizarre question of "whether they should continue trying to sell their product, or switch to a business model

in which the information is literally given away." As IBM Consulting Group managing principal **Larry Prusak** explains this conundrum, "the answer is not obvious. There are virtually no models for thinking about the economics or pricing of knowledge products and informational products delivered via the Internet. So we see some people essentially giving it away, trying to charge instead for ancillary services, while other people are groping around trying to figure out what they can charge for the value they are adding. It's not easy."

Every industry has its own e-business challenges. In the insurance industry a service that used to cost ten dollars per policy now costs fifty cents, and occurs many times faster than it used to.



"We have eliminated an entire function and vastly improved customer service."

Edmund F. Kelly
president and COO,
Liberty Mutual Group

Liberty Mutual Group president and COO **Edmund F. Kelly**, who is on the buying end of the service, is ecstatic at the result: "Insurance underwriting requires the services of an outside credit database company. This has been time consuming and expensive, roughly \$10 a hit. Today, insurance applications are fed into an online system that connects to the credit database for less than 50 cents. That application is then scored by an expert system, and if the risk is sufficiently low, the system automatically produces an insurance policy. We have completely eliminated an entire function and vastly improved customer service."

How to Provide a Service You Can't Provide

For many industries, the new business model demands that companies offer their customers services that the company has never offered before. "There is a new logic emerging," explains **James Moore**, founder and partner of GeoPartners Research. "It is a logic of working with others. In a global and electronically-connected economy if you do not add unique value, you can be commoditized very rapidly. So it becomes necessary to admit that you cannot do it alone. The new logic of competition sees each business as an economic system, a 'business ecosystem' that uses partnership and alliances to cross the old boundaries and take its owners and employees into new businesses far beyond their old core competencies."

The 1997 Business Week Executive Briefing: Connections



"There are virtually no pricing models for knowledge products delivered via the Internet."

Larry Prusak
managing principal,
IBM Consulting Group



"In an electronically-connected economy, you can be commoditized very rapidly."

James F. Moore
founder and partner,
GeoPartners Research



Michael W. Janes
vice-president,
marketing, logistics,
electronic commerce,
and catalog, Federal
Express Corporation

UPS and Federal Express provide examples. "The FedEx website is now linked to about five thousand other businesses' websites," says **Michael Janes**, vice-president, marketing, logistics, electronic commerce, and catalog for Federal Express Corporation. "These are FedEx customers who place FedEx tools directly in the hands of their customers. Companies of every size can now have their own worldwide package delivery network."

In the case of UPS, **Mark Rhoney**, who is the company's vice-president for strategic marketing and e-commerce points out that "it goes way beyond package tracking. UPS will answer your phones for you. Take your orders. Run your warehouse. Pick and pack. Ship (of course), and then do your after-sales service. It is hard to say where the electronic commerce ends and the logistic and delivery service begins."

Toward the Website That Has Everything

There are a few CEOs out there — and the number is still just a few — who have embraced e-business with enthusiasm. "Come to our website!" says Marshall Industries CEO and president **Rob Rodin**. "You can search over 400,000 part numbers! We can interface with you in 24 languages and curren-

cies. We run 30 different websites to address anybody's issues. We have extranets that permit every business partner to go behind our firewall and look at the business that they do with our company. We do this all 24-hours a day, not just technologically: When things go wrong in the middle of the night there is a human being, a warm interface to talk to. It's not press one for this, press two for that, and leave a voice mail. And, of course, we still have to be the low-cost provider."

Marshall Industries is a \$1.2 billion electronics distributor. Rodin reports that only 20% to 30% of his customers are taking advantage of the company's plethora of online services, although "that number is rising all the time." Currently the system

is accessed about 8 million times per month.

At Marshall, Rodin himself drove the change. At companies where the CEO is not so technologically enthused, the challenge falls to executives who must justify their every dollar of investment.

James F. Kessler, III, director of global electronic commerce and director AMPeMerce Solutions at AMP, Inc., reports that his initial investment was \$1.5 million, "and I was forced to justify that at least three times over before the corporation would allow me to go ahead. But that is not a bad thing. My



"Always look for hard, real dollar returns from your Internet investment."

James F. Kessler, III
director of global
electronic commerce,
AMP, Inc.; director,
AMPeMerce Solutions

advice to anyone trying to enter e-business is to always look for hard, real dollar returns from cost reduction and enlarged market presence. Place responsibility for the success of your Internet endeavors in the appropriate hands. You must have accountability for the money that is being spent to get up and running. Clearly articulate your Internet vision and be sure your plan includes education for middle management. All executives must understand the full potential. Test your vision. Share it with your trading partners and make sure they see the same value and benefits that you do. Try it out in a pilot, measure your progress, and demand results. Expect some pain," says Kessler, "and start today." The AMP website has become one of the most successful business-to-business sites on the Internet. It has 108,000 registered users in 138 countries.



Mark Rhoney
vice-president,
strategic marketing
and e-commerce, UPS



Andrew Thomas
director of operations
planning, Heineken USA

HOW HEINEKEN BEAT BUD!

"Heineken is distributed by an independent network of 450 distributors around the U.S., and our competitors — Bud, Miller, Coors, and other domestic brands — control that system. We have 2% of the beer market and we are at the whim of our competitors.

"To improve our share of mind, we created 'HOPS,' the Heineken Operations Planning System, a collaborative forecasting system. HOPS is available to all our distributors over the Internet. It has taken down the barriers. Everything is now visible and collaborative, and all our distributors need is an Internet connection and a browser. We are the only company using the Internet this way in the entire beer industry. HOPS is almost like a video game. We tried to make it that easy for our distributors because we want them to focus on our brands. The distributor who logs onto HOPS sees distributor-specific information. They see a calendar that is so customized to them that we will even put the distributor's wife's birthday on the calendar. That is the kind of relationship that can now be achieved with technology."

Andrew Thomas
director of operations planning, Heineken USA



Robert Rodin
CEO and president,
Marshall Industries

WON'T TAX INTERNET SALES! and other thoughts of Jack Kemp



Kemp
Republican
-Presidential
candidate; co-director,
Power America

"We are at the epicenter of a global business revolution. Two or three years ago there was only \$400 or \$500 million dollars of business being done over the Internet. Today it's a couple of billion, and in another decade tens of billions of dollars. We should not be taxing e-business over the Internet. Some of the governors are worried

their sales tax revenues will fall if an untaxed Internet becomes a principal locus of product sales. Well, Internet sales are going to be cheaper, so they are going to stimulate business. Anything that stimulates business builds a bigger pie. There will still be a revenue base for the states from the income generated by those growing businesses. It's not only business that will be moved by this revolution, governments, too, will be moved — and removed."

Is Business Disintermediated? or Just Intermediate!

The 108,000 users include many who used to buy AMP products through distributors. Today, they buy direct from AMP. What becomes of the distributors who used to serve them? "Disintermediation," says **Steve Smith**, vice-president of consulting, global supply chain services at IBM. "Disintermediation depends on who has the power — who has the information in a supply chain. If you are a manufacturer and don't have a lot of information about the end-user customer, it's probably not a very good idea to try and jump over your distributor. Most manufacturers have spent enough time getting the good, end-user oriented information they need." It is difficult to determine how far you can go in your value chain utilizing your website to touch customers before you start to disrupt your existing channel strategy," warns **Karen Riley**, regional manager for IBM's business process management consulting service. "Integration with suppliers and other partners is the key to success. Integrate the value chain along with your partners, and make yourselves with more information than you had before, and work together."

Professor Michael Zack of the Management Science Group of Northeastern University reports that "disintermediation is being accompanied by reintermediation, which tends to be accomplished by a bunch of different, smaller players who come along with marketplace information that the disintermediating players need. They come out of the woodwork, analyzing the value chain in every industry and asking 'where are the possibilities for reintermediation? Where can I play a role?'"

The Net Will Make Us Honest

"The good news is that the net will make people honest," says **Esther Dyson**, president/owner, EDventure Holdings; and chairman of the Electronic Frontier Foundation. "Your employees are going to be more ornery: It's going to be easier for them to get onto the net, post their resumes, and find another job. Your customers can talk back to you on the net and they can talk about you on the net when you're not there."

"The challenge is to take these lemons and make lemonade out of them. Be the best employer on the block. Have a company that consumers will mostly talk about in a favorable way. Understand



"Understand that you are going to be more visible and more transparent."

Esther Dyson
president/owner,
EDventure Holdings;
chairman, Electronic
Frontier Foundation

that you are going to be more visible and more transparent; so be sure to be a place where employees want to work and consumers want to shop.

"You have to start walking the walk, because just talk is going to be disclosed if that's all it is. You cannot hide behind your advertising message, you cannot hide behind your lawyers, you cannot hide behind your distributors, because your customers are going to come and want to talk to you directly. No matter what business you are in, you are about to own your own retail distribution."

BusinessWeek
EXECUTIVE PROGRAMS
Beyond news. Intelligence.

The 1997 Business Week Executive Briefing: Connections

EXECUTIVE OPINION ON THE INTERNET AND e-business

Every e-business pundit agrees that top-level support — the active interest of the CEO — is important to the success of any Internet website initiative. More than three-quarters of the companies represented at Business Week's CONNECTIONS gathering are already online and the 100 executives who participated offered their own views anonymously through an on-site polling system provided by Meridia.

For a complete report of the briefing's poll results, visit the Business Week website at www.businessweek.com/ebusiness.

POLL RESULTS

Can your customers interact with your company via the web today?

Yes:	74%
System in development:	21%
Still thinking about it:	5%
No, and we won't:	0%

Are you conducting business-to-business commerce over the Internet?

Yes:	53%
No:	47%

I need one-to-one individualized marketing to each customer:

Yes:	67%
No:	33%

What will be the central driver of the Internet as a distribution channel during 1998?

Cost reduction:	60%
Customer value creation:	40%

*Wireless in-hall polling by Meridia,
Plymouth Meeting, PA*



STRATEGIES

ONE MORE FACE-LIFT FOR PENNEY

It's cutting costs and getting fashion into stores faster

Until recently, J.C. Penney Co. practiced what seemed like a formula for fashion disaster. Weeks after the latest dress design from Leslie Fay or a blazer from Alfred Dunner had hit the racks at Federated Department Stores or Dayton Hudson Corp., they would show up at Penney. That's because buyers for most of Penney's rivals are free to order immediately upon spotting goods they judge to be hits, while Penney's buyers had to follow a ponderous system of first showing potential new product to store managers. Only after taking orders from those managers could

they place them with fashion houses.

The resulting delays help explain why the nation's largest department-store chain has suffered three years of weak sales and earnings. Now, CEO James E. Oesterreicher is vowing to get merchandise into stores faster and more efficiently with a new buying strategy. Penney began implementing in February. And he's not stopping there. The Plano (Tex.) chain has embarked on a plan that includes sharp cost-cutting and improved inventory management—all designed to squeeze the most out of a department-store franchise with few

NO-MAN'S LAND? Oesterreicher insists Penney can succeed in the tough middle market for clothes

growth prospect. Last month, Penney reported paltry 0.2% gain for fiscal 1997 net income, to \$50 million. Revenue rose 30%, to \$3.6 billion, but most of the gain came from Penney's drug

stores, which have emerged as the engine that will drive the company's growth into the next century (page 88). Steve Kernkraut, an analyst at Bear Stearns & Co., expects department-store sales to rise a mere 2% on a same-store basis this year.

Penney's department-store unit, which includes 1,200 outlets and the nation's largest catalog operation, has been slow to cut costs, move inventory, and attract top designer labels. It also doesn't help that Penney's stores are caught in a kind of retail no-man's land. More and more, shoppers are gravitating to discount counters such as Wal-Mart Stores and Kmart or high-end retailers such as Neiman Marcus and Saks Fifth Avenue, abandoning retailers that cater to middle-income consumers.

LOOSE THREADS. But even if its sales growth is constrained, Penney has lots of room to improve its bottom line. Its department-store operating margins, 6.7% last year, are the lowest among major rivals, such as Dillard's Inc., 12.1%, and May Department Stores, 12.2%.

Oesterreicher, 56, is aiming to close that gap. Last fall, he offered voluntary early retirement to department-store managers. Some 1,250 of those asked to take the package, or about 80%, did so. The program should result in annual savings of \$85 million. In January, Oesterreicher laid out plans to close "underperforming" stores and slash 4,900 jobs, or 2% of Penney's workforce. That's expected to save an additional \$105 million a year.

Penney is also attempting to get a better grip on purchasing and shipping. The new buying policy will consolidate purchasing functions at its headquarters for 50% to 60% of its stores' merchandise. John T. Cody Jr., president and chief operating officer for Penney's stores, merchandising, marketing, and catalog, says store managers will still buy the other 40% to serve local demographics.

The centralized buying strategy, Cody says, will typically save about four to five weeks. Penney also has substantially improved its fashion offering by adding private and national brand



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The Corporation

in recent years. But it still lacks top labels such as Liz Claiborne, Ralph Lauren, and Tommy Hilfiger, some of which appear in rival Dillard's, May, and Federated. This summer, for instance, Penney will roll out Crazy Horse, a private line of misses' sportswear designed for it by Liz Claiborne Inc. But Liz Claiborne CEO Paul R. Charron balks at giving Penney its signature line for fear of diluting the brand.

SALE CITY. By making earlier commitments, Penney's buyers should be able to negotiate lower prices. And Penney is working to cut its high inventory levels, which have forced it to take aggressive markdowns to clear merchandise. Penney already is doing a better job of predicting sales levels: Inventory at the end of the fourth quarter was down 4% from a year earlier. That helped push department-store operating income up 42% for the quarter, to \$663 million. "They're not giving away the store anymore," says Donald E. Brown, an analyst for Public Employees' Retirement System of Ohio, a big Pen-

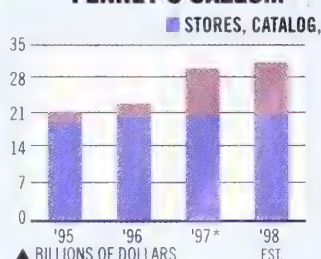
ney shareholder. The moves won't put Penney's margins on a par with Dillard's or May's but should lift them over 8% this year, says Bear Stearns's Kernkraut.

This is familiar territory for Oesterreicher, a 34-year Penney veteran who started as a management trainee in 1964. In the early '90s, while he was head of stores and catalog sales, the company hit the skids after a push into higher-priced goods coincided with the 1990-91 recession. Net income plummeted from \$577 million in 1990 to \$80 million in 1991. It recovered to \$1.1 billion in 1994 on a winning lower-price,

where it had been stuck for 3½ years. The boost came mostly from Penney's job cuts and store closings. But others wonder why it has taken so long. "I think Penney sat around on the success they achieved in the early '90s, while the world changed around them," says Tom Kreisel, chief investment officer at Putnam Investment's Basic Equity Fund, a shareholder. "They were slow to make changes, and now they are having to spend a lot of time playing catch-up. For Oesterreicher, the trick is to make sure that this time, Penney stays fixed."

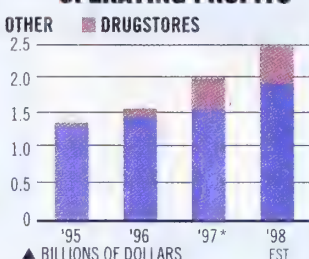
*By Stephanie Anderson Forest
Plano, Tex., with bureau reports*

THE ECKERD DEAL LIFTS PENNEY'S SALES...



DATA: J.C. PENNEY CO.; BEAR, STEARNS & CO.

...AND GIVES A SHOT TO OPERATING PROFITS



*ECKERD CORP. ACQUIRED FEBRUARY, 1997

DRUGS TO THE RESCUE

For 26 years, J.C. Penney Co. saw its Thrift Drug stores as a nice business to be in, but basically a sideshow to its department stores and catalogs. Then, the industry began consolidating in the mid-1990s. "We had to make a choice: Get out, or grow the business," says Penney CEO, James E. Oesterreicher. Penney chose the latter, winding up a two-year drugstore-buying spree with the February, 1997, purchase of Eckerd Corp. The \$3.3 billion deal catapulted Penney from the No. 8 drug chain to No. 4.

It could be Oesterreicher's best bet ever. After exhausting expansion opportunities in department stores—including a failed bid for Dayton Hudson Corp. in 1996—he believes drugstores will fuel Penney's top-line growth for years to come. Eckerd's same-store sales are expected to jump 8% this year, compared with 2% growth at Penney stores. "Eck-



ECKERD: The chain is Penney's new growth engine

erd is making up for some of the disappointment in the department stores," says Blake H. Burdine, an analyst at USAA Investment Management Co., a Penney shareholder.

Still, the strategy is not without risks. Penney's drugstore operating margins are smaller than those of its department stores—5.8%, vs. 6.7%. For now, Eckerd is buying market share—size, after all, is considered

crucial in dealing with managed-care programs. In turn, those programs are squeezing drugstore margins and forcing chains to operate more efficiently. Penney cut costs at its drugstore division by \$60 million in 1997, but margins will likely remain under pressure.

DRIVE-THROUGHS, TOO. Sales growth at the 2,778-store Eckerd chain, meanwhile, is getting a boost from new-store openings and relocations out of strip-mall centers into larger, freestanding outlets. In 1997, Eckerd relocated or opened 200

new-format stores, which include drive-through pharmacies. In time, nearly all Eckerd stores will be converted. Eckerd Chairman and CEO Francis A. Newman says the converted stores are averaging 30% sales growth after their first year. With those numbers, Penney's former sideshow is now stealing the show.

*By Stephanie Anderson Forest
Plano, Tex., with bureau reports*

BY NEIL GROSS

ANXIETY FROM HIGH-DEFINITION TV

THE WIRELESS UNIVERSE EXPANDS, WEIRD NEW CASES of electromagnetic interference are surfacing. On Feb. 1, immediately after WFAA-TV in Dallas began its first transmission of high-definition television, 12 pocket-size heart-monitoring devices used by patients at nearby Baylor University Medical Center went on the blink. The devices relay electrocardiogram signals to a central station, where nurses monitor the patterns on computer screens. The nurses became alarmed when screens they were watching repeatedly went blank. Troubleshooters quickly traced the problem to the HDTV signals, which occupied the same slice of radio spectrum as some of the older heart monitors used at the hospital. No patients were affected, and WFAA halted broadcasts while the hospital replaced the old monitors. But the incidents of this sort seem likely as HDTV and other forms of wireless digital communications proliferate. This year, equipment at a cable-TV facility in Virginia was thrown out of whack by emissions from microwave ovens at a fast-food restaurant. Cell-phone signals have been known to cause interference at cable-TV facilities as well as disrupting antilock brakes and other electronic systems in cars. □

THAT'S BIG R HEAD

TRIPLEGICS WERE THE target audience for this product (photo) from Video Computer, a PC maker in Italy. The headset uses infrared transmitters and receivers to detect movement



OF NOD: Gamers using the UR Gear headset to point and click

the wearer's head and translate that motion into on-screen cursor movements. In the U.S. market, however, Video Computer hopes to compete over a different audience: computer gamers. Their challenge is having to

execute dozens of commands at high speed with just 10 fingers. Whether they use a joystick or keyboard, gamers often rely on one set of finger motions to move through 3-D space on the screen and a separate set to change the view. The headset, which replaces a joystick in any PC game, will eliminate at least one of those command sets.

To look left—whether your character on the screen is standing still or creeping forward—all you need to do is rotate your head slightly to the left. In flight simulations, the headset will make it easier for pilots to keep an eye on the enemy while maneuvering their mock planes in game space. The headset also comes with a microphone, so gamers can talk to their Internet comrades while killing their foes. UR Gear will retail for \$99 when available in the second quarter. *Paul Eng*

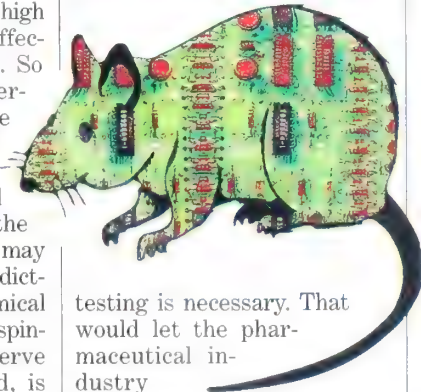
A GOOD DAY FOR LAB RATS

IN TODAY'S AUTOMATED LABS, drug researchers can produce thousands of compounds that promise relief for various diseases. But about 98% eventually fail due to toxicity, high production costs, or ineffectiveness in human trials. So the challenge is to determine which candidates are in the other 2%.

Soon, artificial-intelligence software developed by Multicase Inc. and the University of Pittsburgh may improve the odds by predicting the toxicity of chemical compounds. Multicase, a spin-off of Case Western Reserve University in Cleveland, is now working with the Food & Drug Administration, which is compiling toxicity databases drawn from hundreds of animal studies. Combined with the AI software, the databases will serve as "virtual animals" for screening new drugs. The first FDA databases, now nearing com-

pletion, are designed to help predict which compounds may cause birth defects and fertility problems in animals. Based on that, some compounds could be nixed without costly trials.

These tools won't eliminate the need for lab animals. But they could help the FDA fine-tune decisions on how much



testing is necessary. That would let the pharmaceutical industry slash months or years from its development cycle—thus saving a bundle. Multicase's systems entail a one-time cost of \$56,000 to \$100,000; each animal test series can easily run that much or more. Multicase expects approval of the software within two years. *Johanna Knapschaefer*

INNOVATIONS

■ **Teensy plastic buckshot**—much smaller than the transistors on silicon chips—can be shot into living cells to monitor their biochemistry. The so-called Pebble sensors were developed at the University of Michigan for the Pentagon so researchers could study how biological weapons attack cells. But chemist Raoul Kopelman sees many other uses, including delivering cancer treatments and monitoring glucose levels in diabetics.

■ **Brookhaven National Laboratory** has found a better way to neutralize asbestos: Spray it with a foamy solution that contains special acids. These chemically digest

the asbestos fibers, transforming them into inert minerals that preserve the fire-resistant properties of asbestos coatings. W.R. Grace & Co. plans to market the foam soon. The compound could drastically slash the cost of dealing with asbestos in buildings because the asbestos doesn't have to be removed or replaced.

■ **A steel industry consortium** has uncorked an ultralight auto body to show how cars could lose up to one-third of their heft—yet be even safer in crashes. By using different grades of steel and new manufacturing techniques, the 35-member consortium figures it can shave as much as one ton off a midsize car while doubling fuel economy.

SURGERY

A CATARACT BREAKTHROUGH MAY BE ON THE WAY

A new one-step technique could be a bonanza for tiny Optex

Cataract surgery has come a long way from the days when your local practitioner used a finger to push the clouded lens out of the way—a technique used well into this century in the developing world. Surgical methods have improved dramatically, but conventional surgery remains difficult and expensive—big drawbacks for what has become the most frequent operation of any kind for people over 60.

All of the largest makers of ophthalmic equipment have mounted highly secretive internal programs to find new ways to remove the faulty lens. The companies would not discuss their progress, but surgeons report that Alcon Laboratories Inc., in particular, has licensed technology that would use a heated salt solution to melt the lens. Neither the inventor nor Alcon would comment. Some companies are experimenting with lasers, but those efforts have yet to succeed.

Until the big players are willing to talk about what they are doing, the apparent front-runner in this race is a tiny Southern California company, Optex Ophthalmologics Inc. It has developed a technique called Catarex that requires far less surgical skill than conventional methods. Says Dr. Timothy B. Cavanaugh, an eye surgeon at Hunkeler Eye Center in Kansas City, Mo., who has tried it on a pig: "The rapidity and ease with which I could remove the lens was revolutionary."

FAST AND CHEAP. In conventional cataract surgery, eye surgeons employ an ultrasonic probe to cut the clouded, hardened lens painstakingly into tiny fragments that can be easily removed by suction. Doctors then implant a rigid, plastic lens that partially restores vision. The problem with this technique—called phacoemulsification, or "phaco"—is that it requires surgeons with a high degree of training and skill.

That's why the operation is expensive: Medicare reimburses surgeons about \$1,000 per eye.

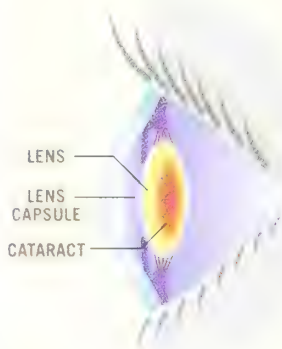
Optex, based in San Juan Capistrano, Calif., was founded in 1990 specifically to come up with a breakthrough cataract device. It licensed its patents to Atlantic Pharmaceuticals Inc., which is now negotiating with big Japanese and

among people who reach 75, the incidence rises to 70%. That translates into 1.5 million cataract removals annually, a number that's growing by 13% a year—and the rate should surge as the baby boomers age. Annual Medicare reimbursements for cataract surgery total \$3.5 billion, the largest single category in Medicare's budget. "We're looking for cheaper ways to do" cataract surgery, says Ellen Lieberman, director of the lens and cataract program at the National Eye Institute, which is partially funding the Optex research. "This is a one-step process, so it's possibly cheaper and faster."

Researchers don't really know what causes cataracts—the hardening and darkening of the clear center of the lens. They speculate, though, that it's possibly caused by exposure to ultra-

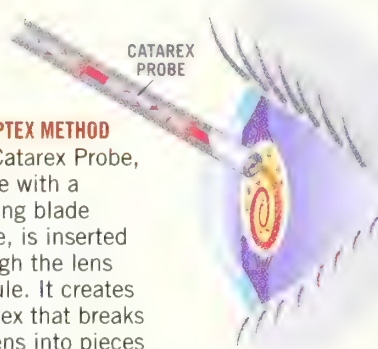
A BETTER VIEW

Cataracts, which afflict some 50% of people over 50, occur when the once clear center of the lens hardens and darkens, possibly due to exposure to sunlight. Eventually, no light can get through, and the lens must be removed in order to restore full sight.



THE OPTEX METHOD

The Catarex Probe, a tube with a whirling blade inside, is inserted through the lens capsule. It creates a vortex that breaks the lens into pieces and sucks them up.



DATA OPTEX

American companies that could take the product through clinical trials and get Food & Drug Administration approval, a process that Optex says should take no more than a year. If the Optex method succeeds, it may even lead to a way to replace lenses for people whose eyesight is weakening as part of the normal aging process, some medical experts speculate.

But even if the technique is used only for cataract surgery, the financial rewards to Optex could be huge. More than 50% of senior citizens will require cataract surgery at some point. And

overt light over a long period of time. Once the darkening begins, new transparent tissue from the outside edges of the lens moves inward and becomes harder and harder, keeping light from reaching the eye's retina. The job of the eye surgeon is to remove the darkened lens and replace it with something that transmits light.

Breaking up the hard nucleus of the lens is the first step in any cataract surgery. With phaco, the conventional technique, the surgeon must maneuver the vibrating tip of the ultrasonic probe—think of it as a tiny jackhammer

If Optex succeeds, cataract removal won't require a highly skilled—and highly compensated—surgeon



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mer—around the nucleus to carve it into tiny pieces. The Catarex technique uses a specially designed spinning blade called an impeller that draws the lens nucleus toward it so that it can chop it up. It's like an old-fashioned milkshake machine that draws solid chunks of ice cream into a vortex and then liquefies them. "We induce a fluid flow within the lens that draws the material to the probe," says John T. Sorensen, the system's inventor.

This new approach allows the surgeon to hold the probe in a stationary position, instead of moving it around within the lens. Using phaco, there's a chance that while maneuvering the instrument the surgeon may rupture the rear wall of the cellophane-like lens capsule that holds the lens—it happens in about 5% of cataract operations. Once the wall is ruptured, surgeons may have trouble stabilizing the implanted plastic lens within the eye. Plus, with phaco, after they break up the lens nucleus, surgeons must insert a second probe into the eye to remove everything that remains. The Catarex system requires just one step—when the pieces of the lens are removed, everything comes with them. And because of the smaller incision, recovery time should be less.

SOFT LENSES. There's another bonus with Catarex: It can be done through a tiny hole in the lens capsule. That opens up the possibility of replacing the lens with an injectable, gel-like substance instead of a rigid plastic contact lens—something ophthalmologists have long dreamed about. A soft and pliable lens would more closely mimic the eye's natural function, expanding and contracting quickly to accommodate the different focal lengths needed for near and far vision. That way, cataract patients would no longer need to wear special glasses for reading.

What's more, the same flexible lenses could be implanted into middle-aged people instead of the bifocals they now resort to as their natural lenses start losing their flexibility. "I have the feeling that some kind of material is close to being available," says Dale P. DeVore, chief scientific officer at Collagenesis Inc., a Beverly (Mass.) company that has experimented with collagen lenses in animals. "But everyone's project is on the back burner because, so far, there's no technique for removing the lens and leaving the capsule intact." If the Catarex system reaches the market, though, those research efforts could be stepped up. And aging baby boomers could end up seeing more clearly well before they suffer from cataracts.

By Larry Armstrong in Los Angeles

The Environment

BIODIVERSITY

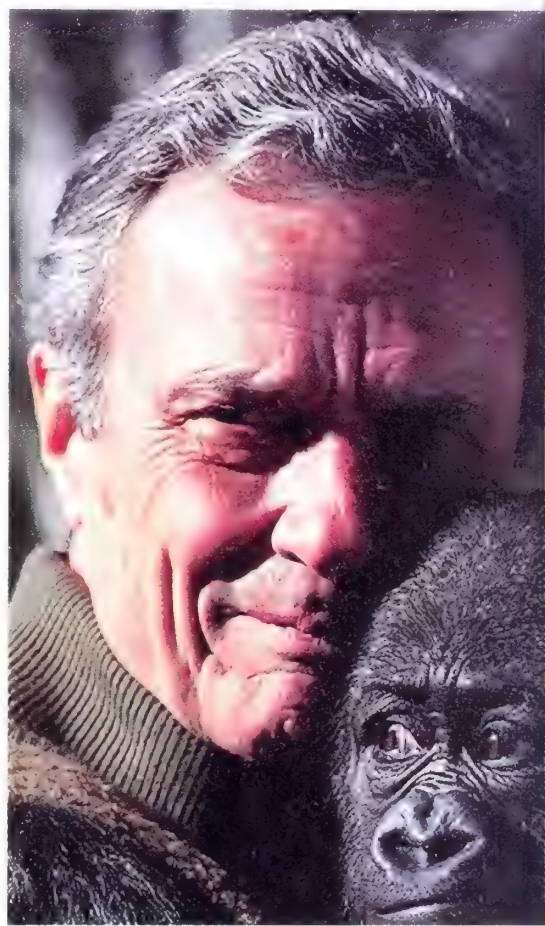
GEORGE SCHALLER'S ECO-CRUSADE

The naturalist is leading the charge to protect species

In the remote Chang Tang plateau of northern Tibet, a few hardy nomads and thousands of antelope, yak, and wild asses roam. With its subzero temperatures and almost year-round snow cover, the starkly beautiful plateau is one of the world's last untouched wildernesses—and, at 125,000 square miles, one of the largest. But commercial interests are coming even to this distant, forbidding place. And the Chang Tang, and its way of life, might not survive.

Each year, to obtain *shahtoosh*, the prized wool of the Tibetan antelope that is woven into shawls for wealthy Westerners, Tibetan nomads and Chinese hunters slaughter hundreds of antelope. If left unchecked, this lust for the rare wool could decimate the antelope and lead to the destruction of the Chang Tang wilderness. For a long time, few knew of the threat to Chang Tang, and fewer cared. No longer, thanks to the interest taken by one scientist. He is George B. Schaller, and his efforts may help avert disaster in the region.

Schaller is one of the world's preeminent field biologists, a naturalist's naturalist who has identified new species, written 11 books, and published dozens of scientific studies. He has blazed a trail for other scientists—he studied gorillas before Dian Fossey did—and when he is interested in a region or species, other biologists follow. His accomplishments include navigating the bureaucratic thickets of China, where he was instrumental in promoting the preservation of the giant panda in the



ANIMAL INSTINCTS

To Schaller, big mammals such as giant pandas and gorillas are emblems for the cause of biodiversity

early 1980s. Schaller also helped persuade the Chinese to begin setting aside 25% of Tibet's land as a nature reserve.

Schaller's new book, *Tibet's Hidden Wilderness*, is but one entry in a vast library of books and films fanning interest in that Asian land. But unlike others who focus on human rights, Schaller is concerned with preserving the mystical and harsh beauty of Tibet's wildlife.

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March of Dimes

March of Dimes - healthy baby

For more information contact your health care provider or call the March of Dimes.

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Schaller and other biologists, there is a pressing need to ensure that the gene pools of endangered species survive, so that their characteristics can be studied. For society as a whole, Schaller makes the case that conserving the diversity of species around the world is critically important because hundreds of species have both documented and yet-to-be-determined value to humanity.

Of the estimated 50 million species on earth, including microbes, fewer than 2 million have been identified. With some species, we may be "too ignorant to measure or know the effect" when they are lost, says Schaller. With others, the loss can have a domino effect, threatening or stunting the growth of plants and wildlife that depend on them. But Schaller says species are worth saving even if they're of no apparent use: Biodiversity "keeps your options open for the future."

At 64, the energetic Schaller looks very much the naturalist—tall, slender, and weathered. Born in Germany, he left with his American mother during World War II and lived for a while in Denmark before settling in the U.S. An only child growing up in St. Louis, he collected birds' eggs and kept a mini-zoo of salamanders, snakes, and opossums. When he got to the University of Alaska, he was delighted to find that he could pursue his interest in wildlife as a field biologist. For the past 45 years, he has studied a wide variety of large mammals in the wild—from the giant pandas of China to the rare mountain gorillas of Zaire. He has tracked Asia's snow leopard and helped identify new species, such as the Tibetan red deer.

"FREETHINKER." Schaller chooses his subjects, whose behavior and habitat he studies for months at a stretch over several years, because they are rare, remote, aesthetically appealing, and biologically interesting. "I want to present a biography of their lives," says Schaller. "That's the first step in understanding, knowing, and helping to protect animals."

For the past 10 years, Schaller has been science director at the Wildlife Conservation Society (WCS), a research and educational organization headquartered at New York's Bronx Zoo. He is admired by many of his peers. "He is one of the great pioneers of field biology of this century," says Russell Mittermeier, presi-

dent of Conservation International in Washington, D.C. "He tackles the most difficult animals to study." Alan Rabinowitz, director of science for Asia at the WCS, regards Schaller as his mentor and hails him as a "freethinker" who "looks for the biological blank spots."

Schaller relishes arduous fieldwork. He has toiled in horrendous conditions, enduring bone-chilling winds in northern Tibet and soggy tent life in the bamboo forests of Sichuan province. His wife Kay, an anthropologist, sometimes accompanies him, as did their two sons when they were growing up. Sick animals—a wart hog and a lion cub in the

will push for the development of sources for short-term economic gain.

Yet Schaller is no firebrand. He believes that any single conservation issue involves "moral ambiguity—you have to juggle principles and practicalities." Schaller notes that more studies are establishing the economic benefits of conservation. According to a recent Cornell University study, ecotourism is worth \$500 billion worldwide, while pharmaceuticals from plants yield benefits worth an estimated \$84 billion.

"CULTURE AND CHARACTER." In the U.S., says Schaller, environmental awareness is greater at the local level

but he finds corporate interest very low. He does reserve praise for specific actions, such as Exxon Corp.'s \$5 million grant to support tiger preservation in Asia. And he lauds wealthy individuals such as media mogul Ted Turner, who is buying large tracts of land in Montana for a nature preserve.

Globally, though, the biggest threat to biodiversity is poverty. The image of local innocents leading

a simple life has long since been supplanted, says Schaller, by the reality of poor people depleting plant and wildlife to earn an income. Villagers should be introduced to

alternative income sources, such as new perennial crops, and governments should be helped to establish reserves. He calls on governments to negotiate limited culling of herds by nomads or villagers.

Preserving biodiversity, says Schaller, is much like ensuring that all the bricks in a wall stay secure. It may be possible to lose a couple, but you can't know when the wall will become unstable. "We still have a large amount of biodiversity," he says. What we need now is the "culture and character" to make the adjustments necessary to preserve the environment and the species that live in it.

Schaller continues to do his part by studying some of those species anew. He's in eastern Tibet this month to survey wildlife. Then, it's on to the forests of China's Sichuan province to track snow leopards, white-lipped deer, and other animals. Later in the year, he hopes to head for the Kamchatka peninsula in eastern Russia, to check in on a bear project. The wild is calling.

By Karen Pennar in New York

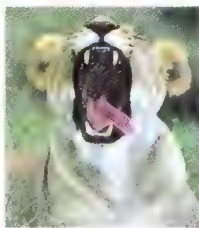
In the Wild: Animals Schaller Has Studied

ANIMAL	REGION	PERIOD STUDIED	EST. NUMBER WORLDWIDE
MOUNTAIN GORILLA	Zaire	1959-61	650
TIGER	India	1963-65	6,000
LION	Tanzania	1966-69	70,000
WILD SHEEP AND GOATS	Nepal and Pakistan	1970-75	NA
JAGUAR	Brazil	1976-79	15,000
PANDA	China	1980-84	1,000
SNOW LEOPARD	Central Asia	1985-	5,000
TIBETAN ANTELOPE	Tibet	1989-	100,000

DATA: BUSINESS WEEK, GEORGE SCHALLER

Serengeti and a peccary in Brazil—were nursed back to health as family pets. "A lot of people would consider camp life a hardship," says Schaller. To him, though, the life most folks lead is a hardship. Phone calls, E-mail messages, and other interruptions "constantly intrude on the pleasure of a quiet mind," he says.

Schaller's accomplishments as a naturalist give him the authority to speak out in favor of conservation and against what he deems to be bad public policy. He lambastes the Clinton Administration for bending to the business interests of Western ranchers who graze their cattle on federal lands at below-market prices. He derides media coverage of threatened species for reducing environmental debates to a simplistic argument over jobs versus animals. And he bemoans the trend toward freer international trade, worrying that multinationals



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EDITED BY AMY DUNKIN

BEATING THE COST OF PRICIER PLASTIC

A good piece of plastic is harder to find these days. Faced with historically high loan losses—in the 6% range—and a record number of credit-card defaults, issuers are raising the costs of the cards in your wallet. “Consumers will have to get used to the fact that interest rates are going to be higher, and they’re going to be given less,” says H. Spencer Nilson, publisher of *The Nilson Report*, an industry newsletter.

Consider that the average annual percentage rate (APR) for figuring interest charges will climb to 19.4% in 1998, up from 16% four years ago, according to Ram Research, a credit-card research firm. Other fees are heading north as well. You may

have to fork over \$25 or more if you make a late payment or exceed your credit limit. Meanwhile, the grace period before finance charges are imposed on your purchases is shrinking—in many cases down from 25 or 30 days to just 20. And some issuers have gone to “two-cycle” billing, meaning you are charged interest for two months instead of one if you fail to pay off your current balance and did not pay interest in the previous month.

Card frills are also being shaved or eliminated. On Mar. 1, NOVUS (a unit of Morgan Stanley, Dean Witter, Discover) pared benefits on a cash-back card that had been among the most generous. Under the old plan, holders of the Private Issue card earned 2% cash rebates on charges above \$5,000. To earn that same 2% now, members must spend at least \$12,000. Spend less,

and the rebate ranges from .25% to 1%. Moreover, NOVUS has instituted a \$500 annual cap on the rebate, where none existed before.

Despite the tightening of the screws, all is not lost if you pay on time, carry a revolving balance, and flash your credit cards regularly. For one thing, it costs issuers about five times as much to replace you as a customer than to keep you, says Lee Spiner, a principal at consultants Booz, Allen & Hamilton. Moreover, Andrew March, director of financial services at J.D. Power & Associates, says that when consumers lower their satisfaction assessments, their spending patterns may be reduced by half. And even with such major players as AT&T exiting the biz, competition remains fierce. (Citibank, which is acquiring the AT&T Universal franchise, says it will honor promises made to customers who were told they would never have to pay an annual fee.)

Indeed, the average cred-

itworthy consumer gets half a dozen or more card solicitations per week, says Michael

Auriemma, president of Auriemma Consulting Group. So you may not have to look no farther than your mailbox for a sweet deal.

Many offerings advertise enticing 4.9% and 5.9% introductory rates. But tease last only a few months before sticker shock sets in, and if you're late with a payment, the rates could triple.

DICKER. Sometimes your current card issuer will make the best deals, says Robert McKinley, president of Ram Research. He adds that you can negotiate to eliminate annual fees and waive late charges. What's more, your card company may have a product that better suits your spending. If you do a lot of business with particular hotels, airlines, or supermarkets, you'd be wise to choose cards they may offer.

You can also dive onto the Net. There's plenty of useful information and gossip at the Ram Research site (www.

What's in the Cards?

CARD	ANNUAL RATE	ANNUAL FEE	COMMENTS
AMERICAN EXPRESS DELTA SKYMILES 800 SKY-MILE	Prime + 9.99%	\$55, or free with another AmEx card	Get one frequent-flyer mile per dollar spent; 1.2 miles if you revolve
CHASE BELL ATLANTIC 800 861-2495	Prime +7.40% for over \$2,500; prime + 9.40% for less	None	Earn rebates of 1% to 3% off your home phone bill
CITIBANK DRIVER'S EDGE 800 950-5114	Prime + 10.40%	None	Earn rebates on any car of up to \$500 a year, \$1,500 maximum
FIRST USA YAHOO! VISA 888 459-2466	9.99%	None	Redeem points at online merchants such as Amazon.com

search.com). You should visit Peter Flur's Credit Goodies page (www.tech.edu/~flur/cards.html) or the Bank Rate Monitor (www.bankrate.com). Meanwhile, the Web's premier search engine, Yahoo!, teamed up with First USA on a new Visa card with a 9.99% annual rate. But be careful: You're late with a pay-
 ment within six months, the rate jumps to 19.99% in-
 terest. The Visa card re-
 wards you with one point for every dollar spent at such online mer-
 chandisers as Amazon.com, Cy-
 berOutpost, and Toys.com. Surprisingly, you can get the card with customer ser-
 vice by E-mail, and a re-
 ward is promised within 24
 hours. You can also get ac-
 cess to the Yahoo! site (www.yahoo.com).

Whether you're hunting for a plastic in the virtual or
 the real world, the ground rules
 haven't changed. In gener-
 al, you'll pay higher annual
 fees and interest rates
 for cards that pro-
 vide cash re-
 bates, points
 toward free

travel or merchandise, and
 other benefits. For example,
 many airline reward cards
 cost \$35 to \$60 a year. Low-
 er-rate cards with no annual
 fees usually come without
 goodies. With that in mind,
 ask yourself how you plan to
 use your credit cards. Are
 you the type who pays the
 whole tab when the bill ar-
 rives? Do you carry a re-
 volving balance?

If you're in the latter
 camp, you'll want the
 lowest inter-
 est rate you can find. Your
 credit union might help. Such
 institutions typically under-
 cut banks by a couple of per-
 centage points, and annual
 fees, if any, are low. The
 downside: Credit unions tend
 to be conservative lenders, so
 you may not get a fat credit
 line. And they aren't known
 for sterling service. "You're
 not going to get a credit-line
 increase at 3 a.m. on a Sat-
 urday," says McKinley.

REWARDS. Wachovia's Prime
 for Life card may make more
 sense for consumers who car-
 ry a hefty balance, despite
 its steep annual fee—\$88 for
 a regular MasterCard or Visa
 and \$98 for a gold version. If
 you fail to make your mini-
 mum payment for three
 consecutive periods, 3.9%
 will be added to the
 prime rate.

Some issuers will

reward you with a bonus for
 carrying a balance. If you're
 an American Express-Delta
 SkyMiles cardholder, you nor-
 mally get one frequent-flyer
 bonus point for every dollar
 charged on the card. But you
 can earn 1.2 points for any
 portion of the balance you al-
 low to revolve at an APR of
 prime plus 9.9%. The Ameri-
 can Express-Delta SkyMiles
 card is free if you already car-
 ry an AmEx card, or \$55 if
 you don't. You'll also earn dou-
 ble miles if you shop with
 such marketing partners as
 Hertz and Hilton hotels. Simi-
 larly, the Banc One Travel-
 Plus Visa card will give you
 one air mile for every dollar
 you spend if you carry a bal-
 ance, or one mile for every
 three dollars spent if you do
 not. And you'll be hit with a
 \$25 maintenance fee if you
 don't accumulate that amount
 in finance charges when us-
 ing the otherwise-no-fee
 cash-back GE Rewards
 MasterCard.

Issuers still lust af-
 ter consumers with the
 fattest wallets. Master-
 Card has targeted the
 American Express crowd
 with its new World Master-
 Card. Like an AmEx card,
 it has no preset
 spending limit
 and offers cer-
 tain travel ben-
 efits. Annual fees
 range from \$50 to \$100. On

the heels of the \$300 AmEx
 platinum card, several com-
 panies have come out with plat-
 inum of their own, though
 none matches such AmEx
 benefits as a free companion
 first-class international ticket
 on some airlines. The newest
 platinum cards are merely
 gold cards with a new coat of
 paint, says David Robertson,
 Nilson Report president. Al-
 though it's keeping mum
 about the details, First USA is
 testing a titanium card
 for the well-heeled
 consumer. But the
 way things are go-
 ing, you will have
 to be very upper
 crust to be able to
 afford plastic the
 color of a metal.

Edward C. Baig

CARD	ANNUAL RATE	ANNUAL FEE	COMMENTS
GE REWARDS MASTERCARD 800 437-3927	Varies, based on credit history	None*	Offers up to \$140 a year cash back
GM MASTERCARD 800 947-1000	18.90%	None	Earn 5% back, up to \$500, to buy a GM vehicle
NOVUS DISCOVER CARD 800 347-2683	Prime + 8.9%; 19.8% for under \$1,000	None	Receive 1% yearly cash-back rebates
WACHOVIA PRIME FOR LIFE 800 716-3000	Prime rate (now 8.5%)	\$88	Cost effective if balances exceed \$3,000

*\$25 fee if yearly finance charges are less than \$25

DATA: BUSINESS WEEK, RAM RESEARCH GROUP

MAKING A BUCK FROM EURO MANIA

The coming of a single currency to Europe next year is sparking a frenzy among investors on the Continent. Amid signs that the euro will force markets to be more efficient and companies to consolidate and restructure, stock markets have soared in the past 12 months. Italy is up 60%, in dollars, and the Netherlands up 30%. But euromavens think their markets still aren't overvalued. "It's exuberance, but it's rational," says Nick Knight of Nomura Securities in London. "Europe has a lot going for it."

The biggest plus: Even traditionally profligate countries have brought their budget deficits down, so long-term interest rates have fallen. Most 10-year bond yields are hovering around 5%. "If you assume this environment will last, stocks look cheap," says Knight.

One way to ride the wave is via mutual funds that track European stock indexes. Despite their good performance over the past year, several closed-end country funds still trade at around a 15% discount to their net asset value, such as the \$100 million Irish Investment Fund (800 468-6475) and the \$103 million Portugal Fund (800 293-1232). An alternative is an open-end fund that spreads its assets among all the major European indexes, such as the \$2.5 billion Vanguard Equity Index European Fund (800 662-7447). It boasts a 12-month total return of 47.6% and a modest expense ratio of 0.35%.

For stock pickers, perhaps the purest plays on the euro

new International Growth Fund (800 426-0107). Jacobson favors "Club Med" players in Southern Europe, where fiscal discipline has improved the most. Among those are Spain's Instituto Nacional Assuranz, Italy's

companies that have restrained so aggressively they likely to remain profitable even if interest rates turn. Omid Kamshad, senior portfolio manager for Putnam's \$2.5 billion International Growth Fund (800 225-1515) likes financial stocks in the Netherlands, Sweden, Ireland, and France. "Valuations [there] aren't stretched yet," he says. His holdings include the Netherlands' ING Groep, Allied Irish Banks, Swiss bank, and France's Soci t  G n rale and Banque Paribas de Paris.

Another beneficiary of monetary union is the software industry. Companies are spending billions to retrofit computer systems to the euro, and information technology providers "are almost all winners," says Jacobson. He owns Germany's SAP, the Netherlands' Getronics, and New York's Mercantile Data. Other service providers are cashing in on the euro less directly. In their drive for competitiveness, more big corporations are outsourcing expensive functions such as food service. James Seddon, who co-manages the \$1.2 billion Rowe Price European Stock Fund in London, is high on French caterer Sodexho and Britain's Compass, which just won a global food-service contract from electronics giant Philips.

With all the euphoria, it's not easy to find bargains. Few companies remain among small caps, says Stephen Beinhacker, senior vice-president at Alliance Capital Management in London. Companies whose fortunes depend on a single currency also are worth a look. Beinhacker points to Spanish oil refiner Repsol, which is restructuring but is trading at just 13 times estimated 1998 earnings, vs. an average of 25.4 for the Spanish market. Even if you're not exuberant over Europe, the Continent is full of opportunities for international investors. Joan Warner



SMART MONEY

are shares in banks and insurers, which are morphing from domestic into regional businesses marketing products in one currency. "The financial sector is going through a process of restructuring that has a lot of potential," says Andrew Jacobson, who manages Pacific Investment Management's

Credito Italiano, and Portugal's Banco Portugu se de Investimento. Besides benefiting from lower inflation and interest rates, they're dumping assets and cutting costs. **TOO HIGH?** Some managers complain that the prices of such southern plays are already stratospheric. Instead, they favor cheaper financial

Stocks for the New Europe

STOCK	PRICE*	INDUSTRY	INVESTMENT RATIONALE
BNP France	67	Banking	Set for long-term profitability
COMPASS** Britain	15½	Food service	Caters to cost-cutting companies
CREDITO ITALIANO Italy	4	Banking	Selling off noncore assets
REPSOL** Spain	46¾	Oil & gas	A bargain in a hot market
SAP** Germany	137	Software	Writing programs for the euro

*Mar. 9, 1998 **American depositary receipt

DATA: BLOOMBERG FINANCIAL MARKETS

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WHERE EGGHEADS PUT NEST EGGS

Want to emulate learned investors? Consider putting money in one of

the no-load, low-expense mutual funds that are now offered by Teachers Insurance & Annuity Assn.-College Retirement Equities Fund (TIAA-CREF), the \$200 billion giant that manages tax-deferred retirement accounts for 2 million current and former faculty and staff members of 6,000 colleges and universities.

The funds, with \$400 million in assets, were launched in September to meet demand from clients who wanted to invest more with TIAA-CREF than their pension plans would permit. Now, those funds

have been opened to all. The funds' records are good—but short (table). Nevertheless, TIAA-CREF variable annuities do have a history. Morningstar Inc. gives three of the group's annuity funds five stars, its highest rating, and three get four stars. "They have below-average risk and above-average returns," says Morningstar analyst Todd Porter. "Over the years, that puts them in the top 25%."

TAX HITCH. The new mutual funds come with some attractive features. One is an unusually low minimum investment for no-load funds, just \$250. Expense ratios are low, too, ranging from 0.49% for the international portfolio to 0.29% for the money fund. That's because TIAA-CREF is waiving an additional 0.5% in fees and guarantees the waiver until July 1, 2000.

The problem in exporting

the TIAA-CREF approach to funds is taxes. Managers for the retirement plans can trade as often they like, since the profits are tax-deferred.

But these funds are taxable, and frequent trading could result in short-term capital gains, which face the same tax rates as ordinary income. TIAA-CREF is aware of this problem. "We're taking steps to minimize tax exposure," says Scott Evans, manager of CREF Investments.

The fund lineup is basic: two domestic equity funds, Growth Equity and Growth & Income; the International Equity Fund; Bonds Plus; the Money Market Fund; and Managed Allocation, which is a blend of the other five. The allocation fund levies no fees, since it invests in others that do. "These are not cowboy funds," says Martin Leibowitz, TIAA-CREF's chief investment officer. "They're not going to swing back and forth

20%—and they're not going to protect you from losses if the market tumbles."

TIAA-CREF's investment approach is a mix of indexing and active stock-picking. At the core of the Growth Equity Fund, for instance, is a portfolio of stocks that acts like the Russell 3000 Growth Index. That's an index of some 1,800 of the 3,000

crepancies. enhanced in a portion of the mutual fund can range from 20% to 80% of its assets.

For the remainder, the manager is free rein to focus on a relatively few stocks—large cap or small cap, growth or value—that he or she thinks will beat the index handsomely. The advantage of the passive approach

is that the index part is always invested, so managers are not forced to buy stocks with incoming cash.

SIMILAR TACKS. The other CREF funds take similar tack but with different benchmarks. Growth & Income uses the Standard & Poor's 500-stock index, and International uses the Morgan Stanley Europe, Australia, and Far East (EAFE) Index. Bonds Plus tracks the Lehman Brothers Aggregate Bond Index and the Plus portfolio can invest in commercial mortgage-backed securities, junk bonds, and even private placements. The 30-day annualized yield is 5.76%—nearly 6 percentage points higher than the average intermediate-term bond fund.

To obtain a prospectus for the new funds, call TIAA-CREF at 800-223-1200, or go to www.tiaa-cref.org on the World Wide Web. Even if you're not interested in

the funds, the Web site is a must-visit. The investment education material is top notch, and it includes primers and scholarly analyses. What else would you expect from an institution that caters to professors? *Jeffrey M. Laderman*

INVESTING

CREF's New Fund Family

FUND	TOTAL RETURN*	
	YEAR TO DATE	SINCE INCEPTION
BONDS PLUS	1.00%	5.55%
GROWTH & INCOME	8.62	17.93
GROWTH EQUITY	10.08	19.10
INTERNATIONAL EQUITY	10.54	8.00
MANAGED ALLOCATION	5.89	11.60
MONEY MARKET	0.98	2.81

*Funds started Sept. 2, 1997. All figures through Mar. 6, 1998

DATA: TIAA-CREF

largest stocks, and they're selected for their above-average price-to-book ratios and forecast growth rates. The fund manager attempts to enhance the index' return by selectively overweighting or underweighting holdings to take advantage of pricing dis-

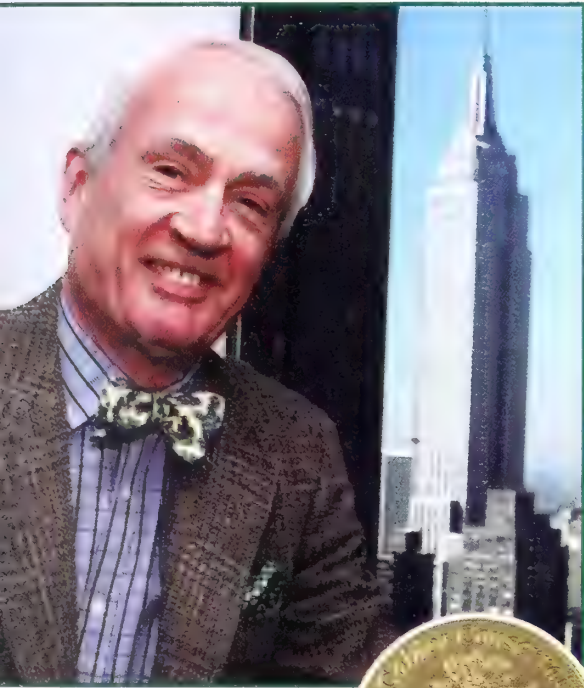
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The Alexander Calder Conservation Award and the Gene Cartledge Award for Excellence in Environmental Education.

We're pleased to present this year's winners, who each receive a \$10,000 grant from Union Camp.



Barney McHenry

ALEXANDER CALDER AWARD

Barney McHenry is being honored for his remarkable accomplishments in New York and New Jersey. As president of the Palisades Interstate Park Commission, he helped spearhead the drive to protect one of the Northeast's most beautiful areas — the Sterling Forest. In fact, his legacy runs from New York City all the way up the Hudson to Albany. The Hudson River Parkway Council — which our winner founded and currently chairs — brings together communities from Manhattan to Albany in partnerships that protect natural resources while promoting compatible economic development. Congratulations to Barney McHenry, winner of our Alexander Calder Conservation Award.



Gracelynn Johnson

THE CARTLEDGE AWARD

Gracelynn Johnson, a science teacher at Camden High school in Camden, New Jersey, is the 1998 Cartledge Award winner. She created and directs an environmental education curriculum that helps her students learn first-hand about the importance of balancing environmental stewardship with economic growth. In one project, her students evaluated a nearby Superfund site and put together a plan to restore the site to productive use. In a second project, Ms. Johnson's students studied the nearby Cooper River and learned along the way how a clean environment is vital to a healthy economy. We salute Gracelynn Johnson for being the tremendous teacher that she is.



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NOW TALK IS REALLY CHEAP

Janice Martin remembers when she'd time her chats with her family back

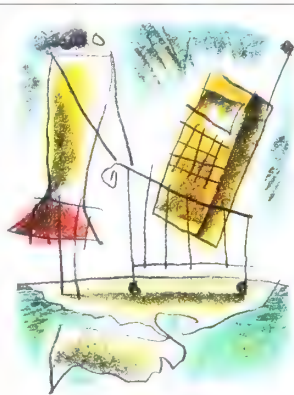
in her native England to keep costs in check. These days, the Washington hair-salon administrator is gabbing with abandon. Her international phone bill is down 33% after switching to an AT&T savings plan in January. "I can call home as cheaply as if I were talking to California," she says.

Martin is a beneficiary of a global long-distance price war. The price of calls abroad from the U.S. fell 25% in 1997, and may drop another 20% a year through 2000. "Everyone's playing the rate game," says John Taylor, senior vice-president at LCI International in McLean, Va., the seventh-largest U.S. long-distance carrier.

SLEW OF RIVALS. Behind the rate war is a big decline in the settlement fees overseas phone companies charge U.S. counterparts to connect calls. Meanwhile, deregulation in the U.S. has allowed thou-

sands of long-distance carriers and resellers into the business, prompting fierce competition.

While you may find slightly better prices with tiny



niche resellers, the telecom giants offer similar rates and attractive options. AT&T, MCI, and Sprint each charge \$3 a month to sign on to their international calling plans (table).

But per-minute rates in these programs are so much lower than the carriers' basic rates that you should consider signing up if you make more than a couple of overseas calls a month. Under AT&T's One Rate International Plan, a call to Japan from the U.S. costs 48¢ per minute, compared

with the basic rates of \$1.10 to \$1.52.

Each of the Big Three's plans has a wrinkle or two that makes comparison shopping worthwhile. Sprint Sense International discounts off-peak calls. So if you're willing to wait until Sundays to dial Britain, say, you'd pay 10¢ a minute, against 12¢ anytime with AT&T and MCI. If you're a traveler, you might like MCI One Interna-

around the globe. If called, charge the call to your number, or if you use it, phone home from abroad, you pay low rates. AT&T has started an Internet billing service, One Rate Online. Right now, it only offers cheap domestic calls. But it's expected to go international by summer. Register at www.att.com.

Smaller carriers may offer better deals than the major

LCI, which does charge a monthly fee, guarantees its low international prices to all users. It also bills calls in seconds, not minutes, to shave more off your tab. Other carriers advertise low rates, but ensure the savings are significant. Sometimes they forgo service such as foreign-language operators.

Even with all the

new discount plans, some international calls remain pricey. It costs \$3.31 a minute to dial North Korea under AT&T's international plan, and that's about \$2 less than the basic rate. Still, phone price gouging will be the exception as most of the world moves toward deregulation and lower settlement fees. "Rates will continue to come down," says Peter Hayden, AT&T's director of global consumer marketing. That's good news for long-distance dialers. *Mary Beth Regan*

Dialing Overseas

	BASIC RATES* PER MINUTE	DISCOUNT RATES** PER MINUTE
BRITAIN	\$0.83 to \$1.14	\$0.10 to \$0.25
CANADA	0.31 to 0.61	0.05 to 0.15
GERMANY	0.86 to 1.31	0.30 to 0.70
JAPAN	1.10 to 1.52	0.40 to 0.77
MEXICO	0.23 to 1.05	0.17 to 0.57

* AT&T

** Based on international plans offered by AT&T, MCI, and Sprint
DATA: AT&T, MCI COMMUNICATIONS CORP., SPRINT CORP.

CALLING

MCI guarantees you the plan's low rates even when you use your calling card in the U.S. or abroad or call collect. MCI rates apply 24 hours a day, too, so you'd save money with this plan over Sprint if you make most calls during peak hours.

AT&T offers several programs. In January, the company introduced its \$4.95 monthly Easy Reach 500 plan. You set up a number with a 500 area code, and calls can be forwarded to you

WORTH NOTING

Interactive Roth IRA worksheets are popping up on the Net. They can help you determine whether to convert an existing IRA to a Roth, which is funded with after-tax dollars, but whose distributions are tax-free. Using a hypothetical conversion, we evaluated several. For more details, go to www.businessweek.com/today.htm or AOL, keyword: BW Daily.

■ **VANGUARD GROUP** (www.vanguard.com). Our favorite. To the impatient, this site may seem tedious: The footnotes and explanations go on and on. But you won't come away

ignorant of the issues. And it lets you adjust the results for some subtle tax liabilities others ignore.

■ **FIDELITY INVESTMENTS** (personal12.fidelity.com/retirement). The site has sufficient explanations, a way of looking at investment outcomes in both nominal and inflation-adjusted dollars, plus the freedom to set your tax rate as high as 60%—good when considering state taxes.

■ **CHARLES SCHWAB** (www.schwab.com). Swifter than Fidelity's, it also had annoying features. For example, it gives you only six preset choices on

the expected return on your investment, ranging from 7.8% to 12.9% a year.

■ **STRONG FUNDS** (www.strong-funds.com). It's quick and straightforward. But this calculator doesn't account for the investment gains you would forgo by paying the conversion tax with money outside of your IRA.

■ **T. ROWE PRICE** (www.troweprice.com). This site was the most sophisticated. Especially helpful: You can see the number of years over which you would liquidate an account.

Robert Bark

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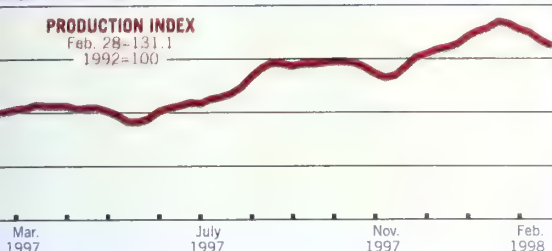
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Business Week Index

PRODUCTION INDEX

Change from last week: -0.4%
Change from last year: -4.7%



The production index continued to slip in the week ended Feb. 28. The unaveraged index also fell, from a revised Feb. 21 figure of 131.6, to 130.3. The monthly index in January was 131.1, down 1.5% from 133.1 in January. Continued rain and mud in Southern California as well as heavy winds and snow in the Powder River caused large declines in rail-freight traffic and coal output. Steel, autos, and production were also down. Trucks, oil, and lumber output posted small gains.

Production index copyright 1998 by The McGraw-Hill Companies

PRICING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STOCK PRICES (3/6) S&P 500	1055.69	1049.34	31.1
CORPORATE BOND YIELD, Aaa (3/6)	6.81%	6.71%	-8.8
INDUSTRIAL MATERIALS PRICES (3/6)	95.9	95.4	-11.4
CRUDE OIL SUPPLY, M2 (2/23) billions	\$4,105.8	\$4,090.9r	6.5
UNEMPLOYMENT CLAIMS, UNEMPLOYMENT (2/28) thous.	304	320	-2.6
MORTGAGE APPLICATIONS, PURCHASE (3/6)	221.1	217.3	25.6
MORTGAGE APPLICATIONS, REFINANCE (3/6)	1,403.4	1,526.1	252.0

Sources: Standard & Poor's, Moody's, Journal of Commerce (Index: 1990=100), Federal Reserve, Labor Dept., Mortgage Bankers Assn. (Index: March 16, 1990=100)

INTEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
MORTGAGE FUNDS (3/10)	5.44%	5.51%	5.21%
COMMERCIAL PAPER (3/10) 3-month	5.49	5.45	5.46
SAVING DEPOSITS OF DEPOSIT (3/11) 3-month	5.58	5.59	5.44
MORTGAGE (3/6) 30-year	7.28	7.22	7.97
STABLE MORTGAGE (3/6) one-year	5.78	5.76	5.78
LIBOR (3/6)	8.50	8.50	8.25

Sources: Federal Reserve, HSH Associates, Bloomberg Financial Markets

Data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

WHAT TO WATCH

Monday, Mar. 17, 8:30 a.m. EST ► Builders expected to have broken ground on new family and multi-unit housing in February at an annual rate of 1.55 million, down from the median forecast of 1.6 million surveyed by Standard & Poor's MMS. The McGraw-Hill Companies. Starts in January totaled 1.53 million.

INDUSTRIAL PRODUCTION

Monday, Mar. 17, 9:15 a.m. EST ► February production at factories, utilities, and mines is expected to have risen 0.2%, says the S&P MMS survey. January production was up 0.2%. The capacity utilization rate fell to 82.9% from 83%.

BEIGE BOOK

Wednesday, Mar. 18, 2 p.m. EST ► The Federal Reserve will release its summary of economic conditions in the 12 Fed districts. The financial markets will be focused on effects of the Asian crisis and tight labor markets. The report is prepared for use at the Mar. 31 policy meeting.

CONSUMER PRICE INDEX

Thursday, Mar. 19, 8:30 a.m. EST ► Consumer prices are expected to have risen in February by 0.1%, based on the S&P MMS survey. That would follow January's unchanged reading. Excluding energy and food, the core index is projected to have increased by 0.2%, the same as in January.

INTERNATIONAL TRADE

Thursday, Mar. 19, 8:30 a.m. EST ► The January trade deficit for goods and services is expected to have widened to \$11.3 billion, says the median forecast from the S&P MMS survey, from December's gap of \$10.8 billion. Exports are expected to have declined, while imports are projected to have increased.

FEDERAL BUDGET

Friday, Mar. 20, 2 p.m. EST ► The February federal budget is expected to have been in deficit by \$39 billion, according to the S&P MMS survey. That would be less than the \$44 billion deficit posted in February of last year.

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (3/7) thous. of net tons	2,216	2,294#	3.8
AUTOS (3/7) units	108,661	111,103r#	-17.8
TRUCKS (3/7) units	150,850	146,859r#	7.8
ELECTRIC POWER (3/7) millions of kilowatt-hrs.	61,959	61,327#	2.6
CRUDE-OIL REFINING (3/7) thous. of bbl./day	14,548	13,847#	7.1
COAL (2/28) thous. of net tons	20,065#	22,663	-9.1
LUMBER (2/28) millions of ft.	494.7#	481.8	2.6
RAIL FREIGHT (2/28) billions of ton-miles	26.5#	27.4	-2.6

Sources: American Iron & Steel Institute, Ward's Automotive Reports, Edison Electric Institute, American Petroleum Institute, Energy Dept., WWPAl, SFPAl, Association of American Railroads

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (3/11) \$/troy oz.	294.100	296.750	-16.3
STEEL SCRAP (3/3) #1 heavy, \$/ton	135.50	140.50	-2.9
COPPER (3/6) ¢/lb.	81.8	77.7	-31.0
ALUMINUM (3/6) ¢/lb.	70.0	68.8	-14.1
COTTON (3/6) strict low middling 1-1/16 in., ¢/lb.	66.10	63.66	7.7
OIL (3/10) \$/bbl.	14.00	15.12	-29.1
CRB FOODSTUFFS (3/10) 1967=100	224.83	221.71	-9.2
CRB RAW INDUSTRIALS (3/10) 1967=100	302.51	302.85	-11.4

Sources: London Wednesday final setting, Chicago market, Metals Week, Memphis market, NYMEX, Commodity Research Bureau

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (3/11)	129.14	126.75	122.43
GERMAN MARK (3/11)	1.83	1.82	1.70
BRITISH POUND (3/11)	1.65	1.65	1.60
FRENCH FRANC (3/11)	6.14	6.10	5.73
ITALIAN LIRA (3/11)	1803.5	1790.7	1693.0
CANADIAN DOLLAR (3/11)	1.41	1.42	1.36
MEXICAN PESO (3/11)	8.660	8.581	7.975
TRADE-WEIGHTED DOLLAR INDEX (3/11)	109.9	109.3	104.8

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars. Trade-weighted dollar via J.P. Morgan

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Monday

Richard Holler of the Association of Shareware Professionals tells how to get the best software cheap, or even free. **Mar. 16**
8 p.m. EST in the BW Enterprise Chat Room

Thursday

Buy, sell, or hold tech stocks? Kevin Landis of ace performer Technology Value Fund gives us the word. **Mar. 19**
9 p.m. EST in BW Online's Conference Room

B-Schools

If you're in the market for an MBA, BW Online has students from the best schools poised for your questions.
Mar. 17: UCLA (Anderson)
Mar. 19: Carnegie Mellon
8 p.m. EST in the BW Online Chat Room

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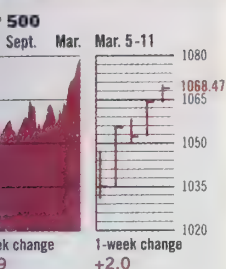
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Investment Figures of the Week

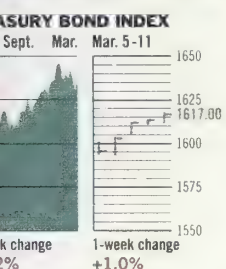
STOCKS



MENTARY

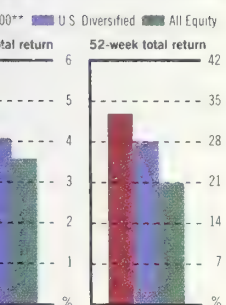
ors went bargain-hunting a tumultuous week. slumped after Intel Corp. d that first-quarter earnings would be below analysts' estimates. The next day, Com-chimed in with similar This time around, however, investors responded to the t's dip by pursuing com- seen as market laggards. w Jones industrial average above 8600 for the first n Mar. 10 and ended the at 8675.8. The Standard's 500-stock index gained at 1068.5. The NASDAQ site fell just 0.2%.

REST RATES



Bloomberg Financial Markets

MUTUAL FUNDS



orningstar, Inc.

U.S. MARKETS

	Latest	% change Week	Year
Dow Jones Industrials	8675.8	1.6	23.2
NASDAQ Combined Composite	1756.9	-0.2	34.7
S&P MidCap 400	360.2	1.8	35.4
S&P SmallCap 600	195.5	0.9	33.1
S&P SuperComposite 1500	229.3	1.9	33.1

SECTORS

	Latest	% change Week	Year
Bloomberg Information Age	319.8	-1.2	34.9
S&P Financials	129.6	3.3	36.2
S&P Utilities	237.5	1.8	22.3
PSE Technology	331.6	-0.5	29.3

FOREIGN MARKETS

	Latest	% change Week	Year
London (FT-SE 100)	5829.8	1.7	31.8
Frankfurt (DAX)	4832.8	2.6	41.5
Tokyo (NIKKEI 225)	16,756.1	-2.0	-7.8
Hong Kong (Hang Seng)	11,118.8	-2.0	-15.2
Toronto (TSE 300)	7345.8	2.8	17.4
Mexico City (IPC)	4742.3	-1.3	26.2

FUNDAMENTALS

	Latest	Week ago	Year ago
S&P 500 Dividend Yield	1.44%	1.45%	1.81%
S&P 500 P/E Ratio (Last 12 mos.)	26.5	26.4	21.4
S&P 500 P/E Ratio (Next 12 mos.)*	20.9	20.5	17.1
First Call Earnings Revision*	-3.88%	-2.49%	-0.93%

TECHNICAL INDICATORS

	Latest	Week ago	Reading
S&P 500 200-day average	945.6	940.2	Positive
Stocks above 200-day average	67.0%	68.0%	Neutral
Options: Put/call ratio	0.57	0.50	Negative
Insiders: Vickers Sell/buy ratio	1.69	1.61	Positive

Data: Bloomberg Financial Markets; *First Call Corp.

BEST-PERFORMING GROUPS

	Last month %	Last 12 months %
HMOs	22.2	Specialty Appar. Retailers 83.7
Genl. Merchandise Chains	16.9	Broadcasting 82.1
Shoes	16.3	Homebuilding 80.6
Building Materials	15.8	Airlines 74.3
Engineering & Constr.	15.1	Manufactured Housing 73.2

WORST-PERFORMING GROUPS

	Last month %	Last 12 months %
Semiconductors	-9.5	Metals -39.2
Computer Systems	-6.1	Gold Mining -33.4
Photography/Imaging	-4.4	Shoes -29.2
Oil & Gas Drilling	-1.3	Photography/Imaging -27.2
Aluminum	-1.2	Engineering & Constr. -24.7

BLOOMBERG MONEY FLOW ANALYSIS

Rebound ahead? Stocks with most significant buying on price weakness

	Price	1-month change
IBM	97 1/2	-5 3/16
Micron Technology	34	-3 3/8
MCI Communications	46	-2 3/16
Texas Instruments	53	-3 3/8
Wells Fargo	321	-6 1/8
Sun Microsystems	42 7/16	-3 3/8

Decline ahead? Stocks with most significant selling on price strength

	Price	1-month change
Microsoft	81 1/2	2 1/32
Dell Computer	65 3/16	10 1/16
WorldCom	37 7/8	1/16
Pfizer	87 7/8	4 3/16
PeopleSoft	48 3/16	5 15/16
Qwest Communications Intl.	37	1 1/4

KEY RATES

	Latest week	Week ago	Year ago
MONEY MARKET FUNDS	5.13	5.13	4.95
90-DAY TREASURY BILLS	5.07	5.19	5.21
6-MONTH BANK CDS	5.08	5.06	5.03
1-YEAR TREASURY BILLS	5.34	5.43	5.71
10-YEAR TREASURY NOTES	5.63	5.76	6.60
30-YEAR TREASURY BONDS	5.94	6.05	6.87
LONG-TERM AA INDUSTRIALS	6.51	6.65	7.38
LONG-TERM BBB INDUSTRIALS	6.98	7.08	7.71
LONG-TERM AA TELEPHONES	6.82	6.95	7.55

BLOOMBERG MUNI YIELD EQUIVALENTS

Taxable equivalent yields on AAA-rated, tax-exempt municipal bonds, assuming a 31% federal tax rate.

	10-yr. bond Latest week	Last week	30-yr. bond Latest week	Last week
GENERAL OBLIGATIONS	4.44%	4.43%	5.04%	5.02%
PERCENT OF TREASURIES	78.86	77.05	84.89	83.10
TAXABLE EQUIVALENT	6.43	6.42	7.30	7.28
INSURED REVENUE BONDS	4.58	4.59	5.24	5.24
PERCENT OF TREASURIES	81.35	79.83	88.26	86.74
TAXABLE EQUIVALENT	6.64	6.65	7.59	7.59

EQUITY FUNDS

Leaders	Laggards
Four-week total return %	Four-week total return %
Lexington Troika Russia 12.8	Lexington Strat. Invmnts. -10.9
Fidelity Sel. Medical Del. 10.6	Oppenheimer Real Asset B -9.3
Safeco Small Co. Stk. NoLd. 10.6	Lexington Strat. Silver -9.2
Firststar MicroCap Instl. 10.4	American Heritage -8.9
Yacktman Focused 10.0	U.S. Global Investors Gold -7.1
Leaders	Laggards
52-week total return %	52-week total return %
Munder Micro-Cap Eqty. Y 69.4	Midas -60.8
Delaware Aggressive Gr. A 69.4	U.S. Global Investors Gold -60.0
MFS Strategic Growth I 59.8	Bull & Bear Gold Investors -58.1
Fidelity Select Air Trans. 58.2	Invesco Strategic Gold -57.6
MFS Mass. Inv. Grth. Stk. A 56.9	Merrill Emerging Tigers B -51.1

EQUITY FUND CATEGORIES

Leaders	Laggards
Four-week total return %	Four-week total return %
Europe 7.0	Japan -3.3
Communications 6.3	Precious Metals -2.9
Unaligned 5.6	Real Estate -2.4
Financial 5.2	Diversified Pacific/Asia -2.2
Large-cap Value 4.5	Pacific/Asia ex-Japan -0.7
Leaders	Laggards
52-week total return %	52-week total return %
Communications 40.2	Precious Metals -41.7
Financial 37.1	Pacific/Asia ex-Japan -35.8
Unaligned 33.0	Diversified Pacific/Asia -24.7
Large-cap Growth 31.5	Diversified Emerging Mkts. -12.8
Small-cap Value 30.3	Japan -6.6

re as of market close Wednesday, Mar. 11, 1997, unless otherwise indicated. Industry include S&P 500 companies only. Fundamentals, technical indicators, Bloomberg mon-

ey flow analysis, and mutual fund returns are as of Mar. 10. For a more detailed explanation, write to us or E-mail figures@businessweek.com. NA=Not available **Vanguard Index 500 Fund

WHAT DO THE TRUSTBUSTERS WANT?

It would be nice if you could just watch your "Herfindahls." In simpler times, companies wishing to merge had to do well on something called the Herfindahl-Hirschman Index, which the Justice Dept. used to measure market concentration. Score above 1,800 and the merger was doomed. Below 1,000, it was legal. Say what you will about relying on such an index, it had the virtue of clarity and predictability. Justice's latest antitrust decisions do not. The largest M&A wave this century may require a more active, vigilant government referee to ensure open markets and competition. But it is incumbent on Washington trustbusters to explicitly state their standards and measurements. This they have not yet done.

What are we to make of the following? Boeing Co. is allowed to merge with McDonnell Douglas Corp., effectively sewing up the domestic commercial-airplane manufacturing market, but doubts are cast on WorldCom Inc. buying MCI Communications Corp. because the combined company might control 50% of the Internet "backbone." Southern Pacific can get together with Union Pacific Corp. to control a major share of the rail lines, but Compaq Computer Corp.'s purchase of Digital Equipment Corp. is questioned. Cable-TV companies can control your access to programming, but Microsoft Corp. shouldn't be able to control access to the Internet. What are the criteria for blocking some deals and not others?

We don't know. The truth is that Joel I. Klein, Justice's top antitrust official, and Robert Pitofsky, chairman of the Federal Trade Commission, are crafting the rules and the rationale for them as they go along. Neither one is a paleo-trustbuster who thinks big is necessarily bad. Each is trying to figure out how to maximize competition in a quickly evolving, global, high-tech marketplace, where huge consolidation is occurring and where new monopolies may be taking hold. It's tough work, but the merger boom can't wait while they cogitate.

Back in the Reagan '80s, antitrust was easy. The market Chicago school of economics infused policy with a simple theme: The only legitimate subject of antitrust enforcement was price-fixing. For a good decade, this translated into virtually no antitrust action by the government.

Klein and Pitofsky belong to a post-Chicago school and wants to do more. Uneasy over the scale of the current merger wave, they believe that there are justifications and beyond price-fixing that require antitrust enforcement. These monopolistic tactics include tying, forcing customers to buy one product to get another (the Microsoft case); exclusive dealing, pressuring distributors to dump competitors' wares (the Anheuser-Busch Cos. case); and standard setting (against Microsoft). In raising objections to the proposed merger between Lockheed Martin Corp. and Northrop Grumman Co., the Justice Dept. said it was acting to "promote competition, protect consumers, and preserve innovation." Good goals, but the country needs to know precisely why this deal is kosher while Lockheed's 19 other acquisitions were fine.

If there is confusion over the competitive rules of the game, the blame must be shared by regulators and politicians. Despite specific legislation, the Baby Bells retain their monopolies in local phone markets by tying up the FCC in court. The cable-TV industry continues to keep out competitors from satellite providers, thanks to an alliance with broadcasters and campaign contributions to friends in Congress.

The New Economy thrives in open markets. The government can help at times by playing referee in a competitive game defined by a handful of clear, simple, and transparent rules. Antitrust enforcement must be predictable and free of the interpretive whims or theories of unseen bureaucrats. It's time for Klein and Pitofsky to set out their New Economic Herfindahls, their standards of competition.

A DISINFLATION HONEYMOON

What is the amazing bull market telling us? Despite predictions of a much slower rise in equity prices for 1999, the Standard & Poor's 500 Index is up a hefty 10%, and the first quarter isn't even over. What ever happened to the Asia crisis? Where's the impact from weak earnings at some of the biggest high-tech companies? What's going on?

Disinflation. Thanks to falling prices, real personal income is taking a surprising turn—upward. Consumers find themselves with greater buying power and their spending is pumping up the economy. The consensus at the end of last year was that this would be a significantly weaker year for growth. Wrong, at least so far.

What's really surprising is how much falling prices are boosting the real purchasing power of consumers. Crude oil prices are down sharply, cutting the real cost of gasoline to

historic lows. Taking inflation into account, gas is cheaper today than it was when cars had fins. It amounts to a whopping tax cut. Prices for computers are plunging as well (page 10). The sub-\$1,000 personal computer is the fastest growing sector of the market, bringing the digital frontier to a big portion of the American population. And, thanks to globalization, prices for imported goods from Asia are sharply lower. Depreciating currencies against the dollar also are boosting the purchasing power of U.S. consumers.

The risk is that price declines get out of hand, and deflation takes hold. A deflationary spiral is crippling Japan, where falling prices are cutting corporate revenues, causing layoffs and drops in income and consumption. But that is just a cloud on the horizon of the strong U.S. economy. For the moment, the stock market is telling people to invest and en-

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MARCH 30, 1998

COVER STORY

WINNERS' CIRCLE

Our second yearly honor roll, culled from the 500 companies in the S&P, is a best-of list unlike any other

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THE BUSINESS WEEK FIFTY

The Business Week Fifty

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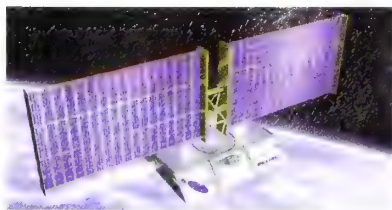
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Up Front

EDITED BY ROBERT McNATT & LARRY LIGHT



HOT BIRD: Satellites are taking off

THE DEAL MILL

HUGHES AND BOEING ARE COZYING UP

GENERAL MOTORS' CLASS H Stock, Hughes Electronics, has been on a rocket lately, climbing 10 points, to \$45, in the past month. Why? According to sources close to the company, Hughes is in serious talks with aerospace giant Boeing.

The substance of the talks, say the sources, is a possible joint venture, merger, or acquisition of Hughes' satellite manufacturing capabilities. Both Hughes and GM adamantly deny that the company is for sale. Hughes CEO Michael Smith terms "pre-

posterous" reports that Boeing has already conducted due diligence reviews.

A business combination centered on Hughes satellite capability could be immensely profitable. Boeing has no such capability now. Douglas Eby, president of Robert E. Torray, an investor in Hughes, says the market is just realizing the huge cash flow Hughes will reap as satellite communications soar. Estimates are that satellite manufacturing alone will be worth \$121 billion worldwide in the next decade.

Both companies already work together. Hughes is set to use Boeing launch facilities for some of its satellites later this year. It is also bidding to supply Teledesic, a satellite communications network that uses Boeing as the prime contractor and will cost \$9 billion. *Seanna Browder*

THE FEDS

SPECTRUM ON THE CHEAP

AS THE FEDERAL Communications Commission prepares to close the bidding on some important unused airwaves, officials can forget about a windfall. In fact, the auction of 1,300-megahertz bandwidth—spectrum that can cheaply transmit phone, Internet, and wireless cable services—looks like it's shaping up to be a letdown.

The FCC is focused more on developing the bandwidth than on raising cash. But Congress expected to raise \$2.5 billion in all auctions for fiscal 1999. The FCC now



McCaw: No. 2

says the ongoing auction has raised only about \$500 million so far. Why? Many investors were wary of the untested technology needed.

On average, top bidders paid just \$1.90 per consumer for the biggest slices of spectrum, sources say. WNP Communications, run by Thomas Jones, looked to win about 35% of the spectrum, with Craig McCaw's NextBand Communications taking 15%. Together, they bid about \$300 million. Both declined comment.

The FCC says that it is pleased the airwaves might finally be utilized. Concludes Chairman William Kennard: "It's not about the money." *Catherine Yang*

TALK SHOW "I thought, 'Well, maybe I ought to just give him a good slap across the face.' And then I thought, 'Well, I don't think you can slap the President of the United States like that.'"

—Kathleen Willey, on 60 Minutes

MUCKRAKERS

LEAVE MY STORE, YOU TROUBLEMAKER

PERHAPS IT'S JUST A coincidence. CompUSA, the nation's largest computer retailer, has given *PC World* the heave-ho from its superstores and pulled its ads from the magazine, which has a circulation of 1.1 million.

PC World Editor-in-Chief Cathryn Baskin says her ad-sales folks told her CompUSA was peeved at two recent unflattering articles. One, in the April issue, bashes its PC repair services. Another, in February, gave it poor marks for in-store salesmanship and online PC ordering.

CompUSA pooh-poohs the idea that *PC World's* stories

influenced its decisions. The chain stopped hawking *PC World* because of low sales. "It's a second-tier product that wasn't selling enough warrant carrying," says CE Jim Halpin. The chain still carries rival magazine *PC*, which has a slightly larger circulation.

As for the pulled ad, Halpin says marketing dollars are better spent elsewhere.

"If we dropped every publication that wrote something unflattering about us," he says, "the only thing we have left [would be] the Bible."

Stephanie Anderson Fore



IMAGE MAKEOVER

THE LADY IS A B-SCHOOL

NO ONE HAS EVER ACCUSED South Carolina of being home to progressive thought. The Confederate battle flag flies over its capitol. Its military school, The Citadel, fought to exclude women. And it has Strom Thurmond.

The image of the Palmetto State, though, may be changing, thanks to one of its illustrious—and wealthy—native daughters. On Mar. 27, the University of South Carolina, in Columbia, will become home to the first major U.S. business school named after a woman



MOORE: Generous

when it is christened the Darla Moore School of Business. Moore, a native of Lake City, S.C., and member of the undergrad class of '75, is donating a record \$25 million to the

B-school. The former banker is president of Rainwater Inc., an investment firm run by her husband Richard Rainwater.

University President John Palms says naming the school for Moore is a step in the state's effort to be more progressive.

"This university has always been the index of the ambition of the state. To name a major business school for a woman is a big deal."

Moore, who got her MBA from George Washington University, agrees. "They didn't have to name the school after me. There

were other alternatives," she says. "But I think they wanted to make a quantum leap in the image they want to portray."

Stephanie Anderson Fore



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A STARTER FUND IN A LEAGUE OF ITS OWN

YOU COULD CALL IT STOCKS for jocks. But its official name is the State Street Research Athletes Fund.

It's a new mutual fund from Boston-based State Street Research & Management, and it's awaiting regulatory approval. Before you ask why the world needs yet another mutual fund, be assured that this one really is different. And very elite. It's designed solely for professional athletes who can invest a minimum of \$100,000. Weekend warriors—even those with \$100,000—need not apply.

Stocks for jocks is designed as an initial investment for younger players who are making a lot of mon-

ey but do not yet have a lot of wealth. The fund will invest in mid- to large-cap stocks and will be managed to minimize investors' taxes.

"By the time they have got \$500,000 or so, they're ready for separately managed accounts," says Derek Sanderson, a State Street executive and former National Hockey League star.

Sanderson won fame as a Boston Bruin before signing a \$2.65 million contract with the now-defunct Philadelphia Blazers in 1973. Like many athletes, he lost it all through poor management and bad investments. Now he wants to help other athletes avoid that sad fate. *Jeffrey M. Laderman*



SANDERSON:
Money man

THE QUIZ TEST YOUR MIDAS QUOTIENT

A group of 78 high-end financial advisers, whose clients have \$10 billion in assets, met at J.P. Morgan in early March to chew on—what else?—wealth management. Morgan polled the group on issues of current concern. Compare your MQ (Midas quotient) to theirs. The answer chosen by the largest percentage of advisers is listed below.

- Over the next 30 days, what type of bonds will perform best?
 - Corporate
 - Mortgage
 - International
 - High yield
 - Emerging markets
- Over the past 10 years, stocks have had annualized total returns of more than 15%. How will they do over the next 10?
 - Better
 - Worse
 - About the same
- When will the Southeast Asian markets turn around?
 - 1998
 - 1999
 - 2000
 - Not in the near future
- The most valuable service these advisers said they gave clients:
 - Getting them organized
 - Asset allocation
 - Security selection
 - Providing discipline to stick to a program
 - Being a sounding board for financial decisions
- In the past three years, these advisers have seen business:
 - Triple
 - Double
 - Stay about the same
- Which movie title describes your practice today?
 - Titanic
 - Clueless
 - As Good As It Gets
 - The Money Pit
 - Grumpy Old Men



BY STAYSKAL FOR THE TAMPA TRIBUNE

TAXES AT WORK

GIVE MONEY OR THIS CHIPMUNK DIES

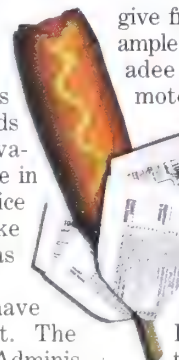
TO THE CERTAINTY OF DEATH and taxes, now add a third item: optional gifts for state spending. Since the first checkoff box appeared on a Colorado tax form in 1977, asking citizens to donate extra funds for wildlife preservation, states have gone in for the checkoff device big-time. Some, like Alabama, offer as many as 12 options.

Taxpayers may have reached their limit. The Federation of Tax Administrators, which represents state tax collectors, found a drop in contributions from checkoff boxes to \$23.4 mil-

lion in tax year 1996, from \$27.8 million in 1992. Why "Sometimes a checkoff will be put on a return because it is the cause of the momer and it outlives its interest," says Neil Allen at Chicago area financial analysts CCH.

Occasionally, taxpayers still give freely. In Kansas, for example, donations to the chickenadee checkoff, which promotes nongame wildlife, rose 22% from 1995 through '96. But usually interest lags. In Iowa, the Corn Dog checkoff, which pays to refurbish the state fairgrounds, raised \$128,000 in 1996.

It has never come close to raising that much again. The fairgrounds are great, say officials. Iowans are just tired of paying extra for greatness. *Roy Furchgo*



THE BIG PICTURE

WINTER WANDERLUST As winter draws to a close, the travel industry is smiling. Americans went on vacations this winter in record numbers, thanks to robust consumer confidence. Cheaper gas prices have helped. And so has a dip in leisure air fares.





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A RANKING THAT REALLY CLICKS

When we launched the BUSINESS WEEK 50 last year, our new ranking of corporate performance, we had three ambitious goals. We wanted our methodology to best identify America's corporate elite—going beyond approaches that rely simply on sales or shareholder return. We wanted the list to be dynamic, believing that year-to-year changes to the roster would themselves tell you something about the economy. Finally, we hoped readers would glean useful insights from our tables that would make their investments more profitable.

One year later, we're proud of what we've accomplished. The 50 companies we identified last year as the top performers in the universe of the Standard & Poor's 500 had price gains of 47.7% for the 52 weeks ended Mar. 13. By contrast, the S&P 500 index gained 34.7% over the same period. The Dow Jones industrial average, meanwhile, rose 24.0%.

As for dynamism, 25 of the companies in this year's top 50 are newcomers. While technology companies still dominate—no surprise there—our screening uncovered less familiar new leaders such as Clear Channel Communications Inc. and Progressive Corp. You'll learn more about those businesses and others in our comprehensive package of stories inside.

To make this year's issue even



1997



1998

more useful to investors, we added a new feature that explains how you can slice and dice the data yourself. If you want to know more, please visit our Web site (www.businessweek.com), where you'll find links to an S&P Financial Highlights Report for each of the 500 companies in the S&P index. And stay tuned. Starting this summer, online aficionados will be able to manipulate the data in a variety of sophisticated ways.

What's behind our success? Quite simply, a ranking system that rewards growth. To come up with our list, we start with the growth rates of sales, profits, and return to shareholders for each company in the S&P 500. We then factor in profit margins and return on equity. To reward consistency, we look at both one-year and three-year results. To level the playing field for larger companies, which have a harder time scoring big percentage gains, we adjust for sales volume. We also rank by industry, so you can see how companies performed compared with their peers.

We're pleased with the results so far. But we're always looking for ways to improve our offerings. So let us know what you think. Meanwhile, happy hunting.

We're pleased with the results so far. But we're always looking for ways to improve our offerings. So let us know what you think. Meanwhile, happy hunting.

Stephen B. Shepard

Editor-in-Chief

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McDONALD'S GIVE A BREAK?

BUSINESS WEEK missed the new news McDonald's USA in "McDonald's: Can it retain its golden touch?" (Cover Story, p. 9). There is significant evidence of improvement in an already strong business. Same-store sales were up in 1997, a trend that continues. Market share grew in '97, reversing a highly reported slight decline. Owner/operator cash flow improved in '97, and management, personnel, and structural changes are starting to have impact.

The investment community is starting to recognize the improvement: The stock price is up over 14% since the yearend. Perhaps others will see the real unfolding and report it.

Jack M. Greenberg
Chairman & CEO
McDonald's USA
Oak Brook, Ill.

Our article indicated that there are really no alumni from the company going to other organizations. There is one major exception: Donald Smith, the chairman of Perkins Family Restaurants and Friendly Ice Cream Corp.

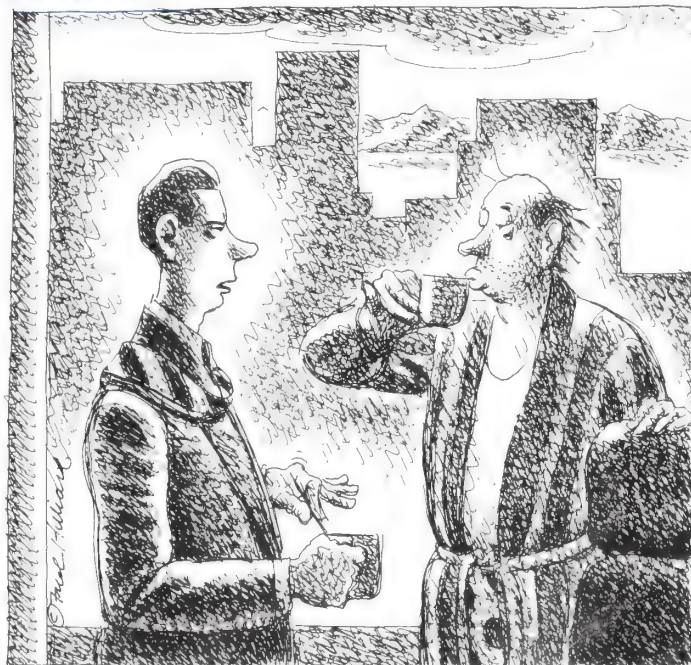
Through the leadership of Smith, who was the former chief operations officer of McDonald's, Perkins and Friendly's are leaders in the family dining segment of the restaurant market. As a result, both Perkins and Friendly's regularly find Smith and his management teams either out in the field working with restaurant operators or in the company's test kitchens devising new

menu items. It is this close attention to customer satisfaction that has permitted Perkins and Friendly's to report revenues and earnings consistently above restaurant-industry averages.

Steven L. Ezzes
Director
Perkins Family Restaurants
Friendly Ice Cream
Westport, Conn.

I am a McDonald's franchisee from Richmond, Va. I have been one for 15 years. McDonald's is the most successful franchising system in the quick-service restaurant industry. As of Mar. 3, we have more restaurants, more sales, more customers, higher average volume sales per unit, higher transactions, and higher profits than any other competitor in our industry. Our nearest competitor, Burg-

WillTales



"While we may differ in degree about corporate casual, Ed, we are as one in the matter of leaving The Big Phone Company for that Williams network."

RECTIONS & CLARIFICATIONS

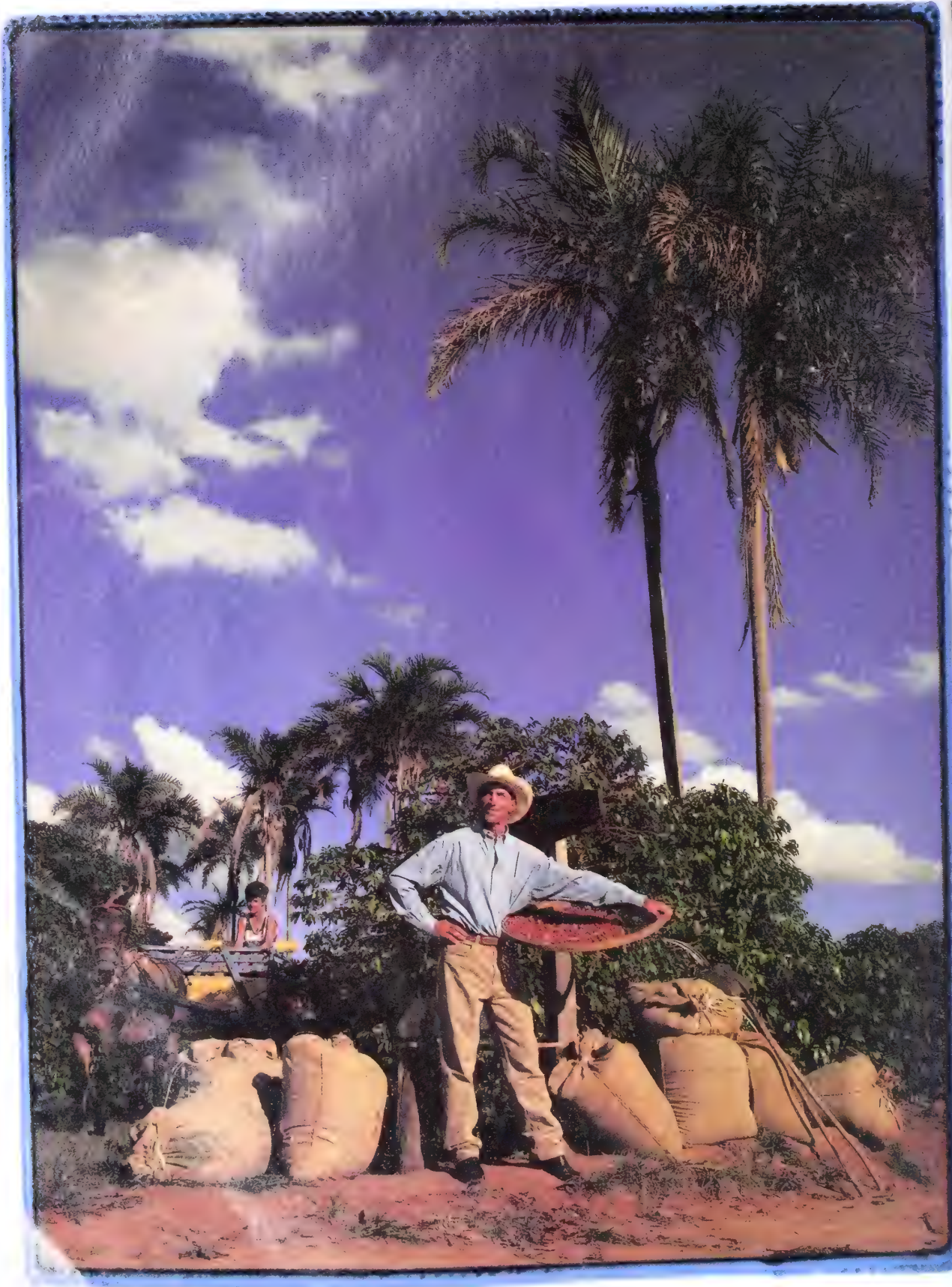
ernance doc, heal thyself" (News Analysis & Commentary, Mar. 16) was incorrect when it described several new rules issued by the California Public Employees' Retirement System. The rules include requiring board members to report all gifts publicly and to open more board meetings to the public. The story incorrectly attributed to Senator Adam Schiff information concerning a real estate investment in which a member's son-in-law has an interest.

time, the Empire may strike out" (Upfront, Mar. 9) erroneously said that Galoob had lost its lead lender. Galoob has established a new line of credit with Congress Financial Corp. Galoob says the three-\$75 million line of credit with Congress is substantially more favorable terms than earlier credit arrangement.

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In Brazil, people will tell you proudly that their country's home-grown coffees are the best the world has to offer. They say that when you sip a cup of their 'cafezinho,' you take inside some of the spirit of their country.

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TOYOTA People Drive Us

Readers Report

er King Corp., has less than one-half of the market share we have.

There are 100 successful owner/operators like me for each unsuccessful, disenchanted operator. Cover both sides, not just the sensational side.

Bill Barnes
Richmond, Va.

I am your normal 13-year-old fast-food customer. My 8-year-old sister and I eat fast food at least four times a week. We don't like McDonald's food or its quality. In fact, it is less than one mile from our house, and we drive past it for other fast-food choices. We also don't think McDonald's is a place that is safe for us to be in or around. Having good food is important, and we are not interested in free toys, playgrounds, or what the brand used to be.

Nik Carlson
Brookfield, Wisc.

I find McDonald's, including the new establishments, to serve tired food in remarkably dirty establishments, served by people with an uncanny propensity for messing up your order after they make you wait for no apparent reason. Chief Executive [Michael R.] Quinlan obviously understands perfectly: McDonald's doesn't have to change; their customers are doing that for them.

Rick Legge
Oviedo, Fla.

McDonald's may be losing market share because of its lack of variety and stronger competition. But the reason my family and friends avoid the golden arches is because of lousy service. Sour employees in unkempt uniforms, dirty tables and counters, and sloppily slapped together Big Macs are the norm.

I worked at a McDonald's throughout high school in the mid-1980s. Back then, we all took pride in our work. Hamburgers were centered on the bun, the fries were never served a minute past their prime, and mistreating a customer meant looking for another job. That pride and service is gone.

Michael Christz
Powder Springs, Ga.

REJECTION FOR INVESTMENT A LEARNING EXPERIENCE

"Henry Kravis...do-gooder?" (Social Issues, Mar. 2) missed a key benefit of the New York City Investment Fund. As the article stated, the fund supplies much-needed capital, provides guidance to deals, and monitors portfolio invest-

ments in the inner city. However, the fund should not be judged solely by the impact of six investments. Ultimately, the benefit to New York will be measured by all of the activities coordinated by the organization.

Many of the 250 unfunded proposals and business plans have received detailed review and feedback from fund sector members, who represent some of the most respected business minds in the world. This commits the scarce resources of counsel, strategic advice, and business contacts to the inner city. The value of the time invested must not be underestimated.

Todd Dubner
New York

THE GSA: NO "IMPROPER INFLUENCE EXERTED"

Once again, the General Services Administration must respond to a story ("The heat under Peter Knight," Government, Mar. 12) about the consolidation of the Federal Communications Commission. This is an 11-year-old effort GSA undertook following authorizations by Congress in 1987 and pursuant to a 1994 federal court order.

What is of most concern is that by piecing together selected events and facts, with a twist of innuendo, the story perpetuates the false impression that actions GSA has taken to consolidate the FCC have been improper or—worse—illegal. No one has ever asked GSA officials at any level to compromise any legal obligation or any personal or professional ethics, nor have GSA officials done so. The lease GSA entered into for Portals II in 1994 was the result of protracted litigation. Neither the terms of that lease nor any of the subsequent supplemental lease agreements with Portals II owners were the result of any improper influence exerted on GSA officials—career or otherwise.

Hap Connors
Deputy Associate Administrator
Office of Communications
General Services Administration
Washington, D. C.

MOTOROLA IS A DIGITAL LEADER, NOT A LAGGARD

Motorola Inc. disagrees with your interpretation of its digital competence ("Wireless goes haywire at Motorola," News: Analysis & Commentary, Mar. 9). No digital wireless competitor competes in as many markets as we do.

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including the largest one ever awarded in Japan. We created the world's fastest growing time-division multiple-access digital-wireless technology, called iDEN(R).

We set an industry record, launching 49 digital TDMA intelligent satellites into space in the past 10 months. This digital wireless "network in the sky" will provide a digital phone call or page virtually anywhere on earth.

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Albert R. Brashea
Director, Corporate Communication
Motorola Inc.
Schaumburg, Ill.

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SPIN CYCLE

The Clinton Propaganda Machine
by Howard Kurtz
Hardcover • 324pp • \$25

HOW THE CLINTONS MANAGE THE MEDIA

From the moment Bill Clinton emerged as a Presidential front-runner in late 1991, his relationship with the national media has been... Clinton views the press corps as... with stories he considers unimportant (his personal life, family financial... his draft history) and insufficiently interested in issues he considers important (his economic plans, his... to reshape the Democratic... into his moderate New Democrat... From the 1992 Gennifer Flowers... frenzy to Kathleen Willey's... appearance on *60 Minutes*, Team... has made a career out of depolitical dynamite.

Clinton's disdain for the media... well-known when I took over the... House beat for *BUSINESS WEEK* in... 1997. But I was surprised at the... corps' hostility toward the President and his staff. Weren't these scribes... liberal media elite" that my friends... "vast right-wing conspiracy" like... about?

Howard Kurtz's *Spin Cycle: Inside Clinton Propaganda Machine* goes a... way toward explaining the enmity... longtime *Washington Post* reporter... a disturbing, enlightening, yet... tely flawed picture of a pair of... ctional families: the White House... s who work to "manage" the me... and the diverse collection of ultra... titative reporters whose job it is to... end The Spin to find The Truth... tzt portrays Clinton as a politician... suspicious of the news Establishment. "They like to destroy people,"... President is quoted as telling ad... Dick Morris. "That's how they get... rocks off." The press, meanwhile... trated that most Americans seem... buying the Administration's view... it's important and what's not.

Kurtz, one of the country's most... red media critics, does a compre-

hensive job of reporting a year in the life of the White House spin machine. For those of us privy to the briefing-room jousting between Press Secretary Michael D. McCurry and press corps agents provocateurs, it is fascinating to discover the maneuvers behind McCurry's carefully scripted word choices—and the battles he often wages to win permission to pass along shreds of information. Relying on anecdotes related by White House spinners and reporters alike, Kurtz describes the White House's favorite tactics: deny the accusations, release as little information as possible, attack the accuser's motives, focus on any inconsistencies, describe the allegations as part of a right-wing conspiracy, and—most of all—change the subject to the economy or some Administration initiative.

Kurtz reveals the lengths to which White House aides will go to attack and discredit Clinton-bashing reporters. Sometimes, this means a personal Presidential rebuke of offending reporters. But in the case of *Washington Post* Whitewater reporter Susan Schmidt, it meant a "frontal attack" on her credibility ordered by Hillary Clinton, according to Kurtz. Although staffers bad-mouthed the reporter, the idea of an official White House report publicly critiquing Schmidt's stories was finally squelched by McCurry, who feared a media backlash.

While McCurry and other White House spinners such as Lanny Davis and Rahm Emanuel are generally given high marks for effectiveness, the President and First Lady are depicted as somewhat naive about the way the game is played. One example: Mrs. Clinton thought a private meeting with

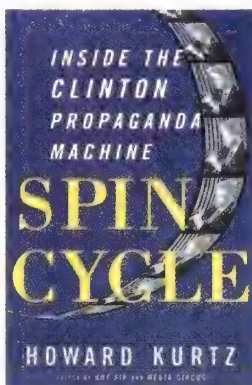
Washington Post Executive Editor Leonard Downie could temper the negative tone of that paper's Whitewater coverage. But, says Kurtz, the session was "a disaster." Her personal touch wasn't enough—Downie kept pressing for documents that could prove her assertions of innocence. "That was the day she knew she was screwed with the *Post*, she told a colleague afterward."

Kurtz's reporting is incredibly detailed, but his analysis is debatable. He devotes too much space to the scandal coverage of the *Post*, *The New York Times*, and *The Wall Street Journal*. Those papers set the tone for much of the White House press corps coverage, but their scoops failed to make much of an impression on Middle America. Kurtz vastly underemphasizes outlets used by the White House to refocus attention away from scandal, including *USA Today*, wire services, and regional newspapers. And Kurtz does not devote sufficient space to TV.

Kurtz's book undoubtedly will prove valuable to academics who in future years will put the Clinton Presidency into historical perspective. And it provides a useful service to contemporaries who want to plumb the depths of the spinmeisters' minds. But it seems a bit out-of-date in this tabloidish moment of Monica Mania. The problem: Kurtz's book focuses on 1997 and

White House attempts to minimize campaign fund-raising and Whitewater allegations. Kathleen Willey, who now claims she was groped by the President outside the Oval Office, makes only a cameo appearance. Monica Lewinsky and Linda Tripp are mentioned only in a hastily added introduction and epilogue. Independent Counsel Kenneth W. Starr is only one of many supporting players in the drama. *Spin Cycle* provides some valuable lessons that will help a reader understand the story behind today's headlines. But if anyone picks it up to get the inside skinny on late-breaking developments, that person is bound to be disappointed.

BY RICHARD S. DUNHAM
Dunham covers the White House for BUSINESS WEEK.



KURTZ SHOWS HOW FAR THE WHITE HOUSE WILL GO TO COURT—OR DISCREDIT—REPORTERS

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COMPUWARE
What do you need most?

BY STEPHEN H. WILDSTROM

WHY MICROSOFT MUST DO BETTER

It may have a point in the browser wars, but it had better fix all those glitches

My Feb. 23 column, which argued that consumers would benefit if Microsoft Corp. is allowed to integrate a Web browser into Windows, attracted a lot of comment from readers. Most of the messages took issue with me, and many of them made me think.

I still believe that an integrated browser is a good idea because, among other things, it makes access to the Internet easier. I even think that the common standard created by the near-monopoly of Microsoft's operating system benefits consumers by forming the basic foundation for software designers. But readers repeatedly raised one important point: Without competitors breathing down its neck, what gives Microsoft an incentive to create the best possible software?

ERRATIC. Microsoft's argument, made in recent Senate testimony by Chairman William H. Gates III, is that dominance in the high-tech business is fleeting. Perhaps the Sun Microsystems Inc.-IBM collaboration on Java software, which is designed to function on all sorts of computers, will make operating systems irrelevant. Or maybe Apple Computer Inc.'s upcoming Rhapsody OS will sweep the market. But while waiting for a threat to Microsoft's reign, consumer wars are justified.

A concrete example comes

from reader Mark Hazell of Halifax, N.S. He needs to read documents posted to the Web in many formats, including Corel Corp.'s WordPerfect, the chief rival to Microsoft's Word. Although a distant second in word processing, WordPerfect is widely used for legal documents, including many in the Justice Dept.'s online archive for the *U.S. v. Microsoft* antitrust case.

Word can read WordPerfect files. If you've told Windows to use Word to open WordPerfect documents, then when you click on a link on a Web page, your computer should launch Word and open the file. Hazell's experience was quite different, and so was mine. When I clicked on the link in Internet Explorer, the browser asked what program to use to open the file. Word then fired up but announced that it couldn't open the WordPerfect file. Netscape Navigator 4.0, by contrast, launched Word and opened the file with no trouble. After a week of phone conversations and E-mail exchanges, Microsoft traced the problem to bad information in the registry database that Windows uses to store information about your computer.

Now, this isn't an earth-shaking problem. The fix,

once found, was relatively simple. And you could always work around the glitch by saving the WordPerfect file to your hard disk and opening it from within Word. But an ordinary customer has little hope of getting as much help as a journalist working on a story. Worse, Microsoft's online help has frequently been unusable because of erratic performance at its Web site, support.microsoft.com. The company says it is in the process of upgrading the site to improve responsiveness.

Unfortunately, Windows annoyances are far from rare. Mysterious crashes and mys-

computer has been reading. Again, I can work around the problem, but it has persisted through two updates of Windows 95 and remains in the test version of Windows 95 **HIGHER STANDARD.** These little glitches add up to a big blind spot. Software may be the only business where companies routinely ship products with known defects, and Microsoft is no worse than many others. But I believe its position in the market gives it a special responsibility. If I don't like CyberMedia Inc.'s UnInstaller utility, I can use Quarterdeck Corp.'s CleanSweep instead. Even

though Microsoft Office has most of the application suite market, I can switch to Lotus SmartSuite or WordPerfect Suite. But in operating systems, especially for individuals, the choice is Windows or nothing.

So what is to be done? It's up to Microsoft to step up to the plate, since the government can neither create competition nor regulate quality. The company can produce high-quality software. Windows NT is sold as an operating system for essential business functions and, not incidentally, faces no competition from Unix. This is one reason it is more

reliable than Win95. Earlier versions are tested more rigorously before release, and "hot fixes" are quickly made available as bugs are found.

Microsoft should be able to do as well for consumers and does for business network customers. We have no choice but to use Microsoft to get where we want to go. They should make it a better trip.



Mysterious crashes and error messages add up to one big blind spot

tifying error messages, such as the dread and almost unfixable "Windows Protection Error," are far too common. For example, nearly every time I install a printer or other device, Windows stops partway through the process and informs me that it cannot find some file that it needs. Almost invariably, the file is on the installation disk the

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BY ROBERT KUTTNER

CURRENCY BOARDS: A BAD IDEA THAT JUST WON'T GO AWAY



PEGGED:
Boards like the one Suharto is planning leave a weak economy at the mercy of speculators

One curiosity of the Asian financial crisis is the vogue for a quirky idea—the currency board. In Indonesia, President Suharto is proposing that the rupiah be pegged to the U.S. dollar, with a politically insulated currency board empowered to set and defend its fixed exchange rate. He is abetted by a U.S. economist, Steven Hanke at Johns Hopkins University, who promotes currency boards as a monetary panacea.

Hanke's plan pegged the rupiah at 5,000 to the dollar—about twice its current worth. The rupiah briefly rallied when it was first suggested. Then, wiser heads prevailed. To put it less politely, the International Monetary Fund and the Western powers warned the old dictator that if he persisted, there would be no IMF aid. It may be the IMF that backs down. Suharto appears to be proceeding.

Currency boards and rigidly pegged exchange rates leave weak economies with an inelastic monetary system that is hostage to someone else's currency. To fortify a weak currency with a pegged exchange rate against speculative assault, there is only one policy instrument. The board must raise domestic interest rates so high that traders start buying the currency rather than shorting it. In the meantime, the high interest rates savage the local economy.

Currency boards and pegged rates have worked in very special circumstances, such as Hong Kong and Argentina. The former is a city-state with a very strong banking system. The latter suffered from hyperinflation and turned to a currency board as part of a package of wide reforms of the sort Suharto has no appetite for implementing.

OVERBURDENED. If currency boards became generalized, the result would be a more rigid version of the fixed-exchange-rate system that prevailed during the Bretton Woods era, until 1973. At that point, the U.S. dollar could no longer anchor the world's monetary system without producing inflation at home. America shifted to a system of floating rates, widely praised as more "marketlike." But if the U.S. economy, which was relatively more prominent in 1971, could not undergird the global money system then, it can hardly do so today.

What is also peculiar is that monetary conservatives, led in this case by *The Wall Street Journal* editorial page, love currency boards. However, if all prices are optimized when they are set by free markets, shouldn't that

logic also apply to exchange rates? Evidently there are times when market forces are perverse. Otherwise, why saddle currencies with fixed exchange rates?

What explains this muddle of first principles by cheerleaders for the genius of the market? It turns out that champions of currency boards hate governments even more than they love markets. The vogue for currency boards is a close cousin to the longing for a gold standard, and to Milton Friedman's call for a "fixed monetary rule." Namely, central banks should stop meddling and put monetary policy on automatic pilot.

STABILITY AND ELASTICITY. Central banks, of course, are already supposed to be insulated, but to some true believers, they are not insulated enough. They come under political pressure to print money. With a currency board and a pegged rate, printing money doesn't help because there must be offsetting hikes in the interest rate to defend the watered-down currency. So interfering in the market by pegging rates paradoxically forces countries to bend to the judgment of markets—in this case speculative financial markets. That can indeed introduce draconian monetary discipline. But the cure is often worse than the disease.

Ironically, it was Keynesians—the fathers of Bretton Woods—who appreciated that the monetary system needs a blend of stability and elasticity. That requires government intervention, shelter from speculative pressure to deflate, and infusions of credit to new cases—not a procrustean fixed rule.

The Bretton Woods system pegged rates and discouraged speculation. It included a collective defense of fixed rates, lubricated by IMF credits. A currency board, in contrast, leaves a weak economy at the mercy of speculators, with all the rigidities of fixed rates and little collective support.

One would welcome more stable exchange rates—in the context of an elastic monetary system that promoted growth. Supporters of this middle ground have proposed a variety of remedies, from "crawling pegs" (fixed rates that are adjustable) to taxes on currency speculation to regional regimes of managed stability, such as the European Monetary System. But the gold bugs and their currency-board cousins propose exactly the wrong combination of free markets and rigid control.

Robert Kuttner is co-editor of *The American Prospect* and author of *The End of Laissez-Faire*.

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BY GENE KORETZ

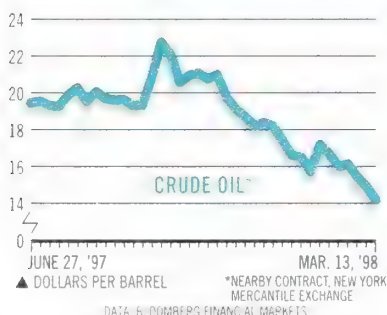
HOW LOW CAN OIL PRICES GO?

Some analysts see more weakness

To U.S. consumers, whose heating oil bills have plummeted and who are paying as little as \$1 or less for a gallon of gasoline at the pump for the first time in recent memory, it's like money in the bank. To commodity traders and analysts, it's a move whose sharpness and speed few anticipated. And to economists, it's a potent new development to factor into their forecasts of economic growth and inflation.

Since October, oil prices on world markets have plunged by a third, dipping below \$14 per barrel for the first time in a decade and touching record postwar lows in real terms. And though

OIL PRICES TAKE A BIG SLIDE



global stocks of oil almost never rise in the first months of the year, they seem likely to surge by a heady 1.3 million barrels per day in the current quarter, says energy analyst Michael Rothman of Merrill Lynch & Co.

A number of factors are contributing to the latest downward price spiral. On the demand side, the most obvious is the turmoil in Asia, which has slashed consumption by some 500,000 barrels per day, and which may not be resolved for many months—or years—to come. In addition, both Europe and North America have experienced unusually warm winters. The U.S. government reports that the first two months of 1998 were the warmest on record in the lower 48 states.

On the supply side, the OPEC cartel actually boosted its production quotas last November, and several members, notably Venezuela and Nigeria, continue to exceed their quotas. And the U.N. is now in the process of raising Iraq's limit.

As for the economic fallout, economists at Salomon Smith Barney estimate that the recent decline in oil prices, if sustained, could reduce consumer inflation in Europe and the U.S. this year by 0.25% to 0.5% from where it would otherwise be. Lower prices also could add about 0.25% to economic growth, cutting the anticipated contractionary impact from the continuing Asian crisis by a quarter to a half.

Not everyone will benefit from lower oil prices, of course. For oil exporters, in OPEC and out, the price drop is a heavy blow. And the collapse of Asian currencies means that for some Asian countries, the price of oil imports has actually doubled or tripled in the past year.

The futures market suggests that oil prices will recover some ground later this year. But energy analyst Richard Redash of Prudential Securities Inc. argues that the disarray in OPEC ranks, the growth in non-OPEC output, and continuing technological advances that are slashing the costs of finding and producing oil (BW—Nov. 3) all suggest that the market still hasn't hit bottom.

Merrill Lynch's Rothman agrees. Without a production cut enforced by OPEC or some geopolitical disturbance that affects the availability of oil, he says, "it's entirely possible that we could eventually see prices retest their 1986 lows of \$10 per barrel."

THE MYTH OF STOCK VOLATILITY

Price swings aren't out of line

With the Dow bobbing up and down like a yo-yo in recent years, Wall Streeters have come to believe that increased volatility is an unavoidable feature of today's buoyant market. In point of fact, however, the increased volatility that's raising anxiety levels is illusory, concludes a new study by G. William Schwert, a professor at the University of Rochester's William E. Simon Graduate School of Business Administration.

Schwert studied U.S. stock indexes at monthly, daily, and intraday intervals and found that returns on investments in any of these time frames over the past decade were not especially volatile by historical standards. Volatility stayed high for a short while after the 1987 crash but then returned to normal levels, Schwert's data show. Only one day in the 1990s—last Oct. 27—made the lists of the top 35 percentage falls or top 35 rises from 1928 to 1997.

That day ranked as the 17th-largest stock market decline. Most of the biggest changes were in the early 1930s.

Why do many traders believe the markets are volatile? One likely reason is that they haven't gotten used to the higher levels of the major indexes, which small percentage changes produce big point swings, says Gregor van Kipnis, chief executive of Invicta Partners, a New York investment manager. When the Dow doubles in just three years and quadruples in a decade, a 100-point rise or drop in a day is what it used to be.

Another reason may be a growing appetite for leveraged trading. Some Wall Street firms, says Schwert, may be taking big risks in markets, so that even modest volatility seems scary to them.

By Peter C.

THE TRADE GAP WON'T BE ALL BAL

Many overseas units may thrive

Although an ominous cloud looms over America's trade balance this year in the form of slowing exports and fast-rising imports, economist Joseph Quinlan of Morgan Stanley, Dean Witter, Discover & Co. spies a silver lining on the import side: the growing role of overseas affiliates of U.S. companies.

In 1995, the last year for which data are available, U.S. affiliates operating in foreign countries accounted for almost a fifth of U.S. merchandise imports, and today that share is probably higher. In last count, it was 81% for imports from Singapore, 52% for Hong Kong, 46% for Ireland, 40% for Canada, 30% for Britain, 26% for Mexico, and 14% for 20% for Indonesia, Malaysia, Brazil, and Thailand (chart).

As imports from Asia and elsewhere rise this year, says Quinlan, a growing portion is likely to come from affiliates of U.S. multinationals benefiting from lower production costs overseas. This trend, he says, "will reflect America's competitive strength, not its weakness, and will mean added profits for a number of parent companies."

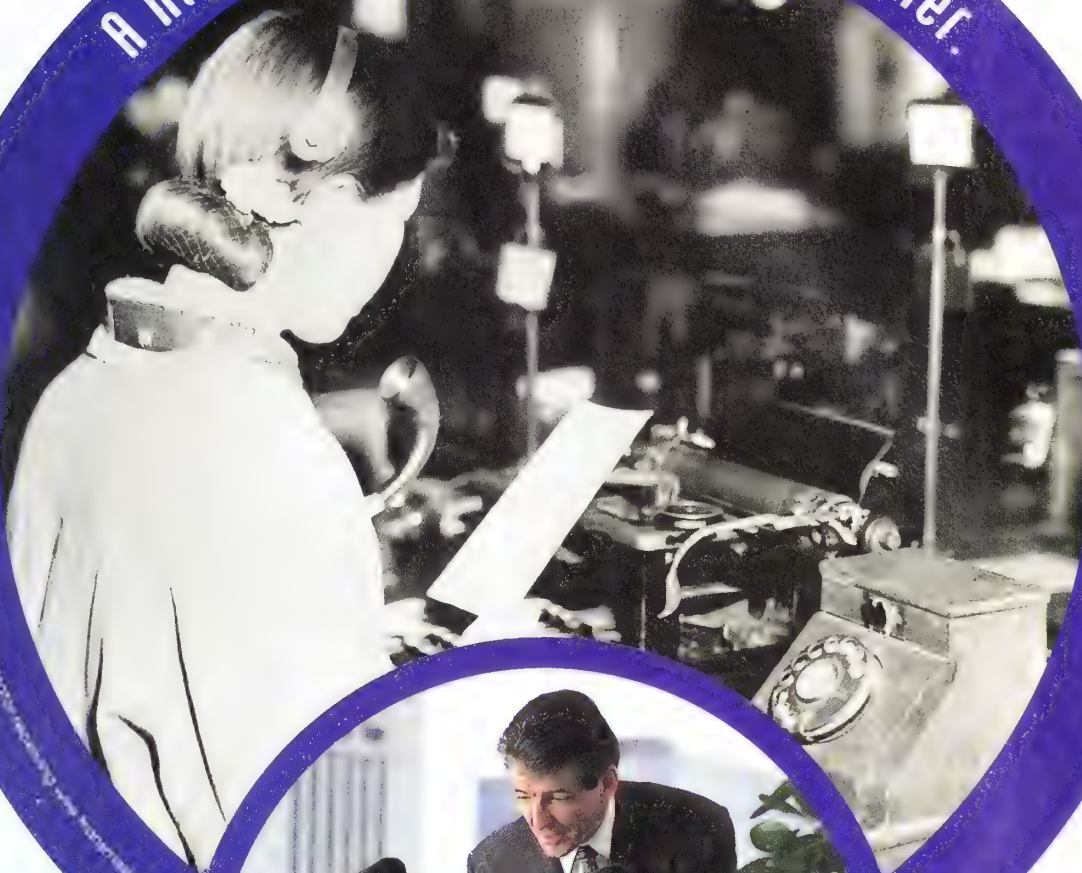
SOME U.S. IMPORTS SPELL PROFITS

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JAMES C. COOPER & KATHLEEN MADIGAN

CONSUMERS' SHOPPING CARTS ARE FILLING FAST

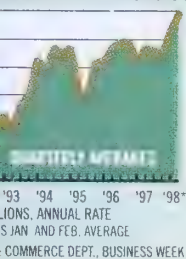
Sound fundamentals and warm weather keep the economy pulsing

U.S. ECONOMY

Buying power: U.S. consumers have it, Asians don't. The main lie in the economy's first-quarter performance. Income growth is surging this quarter, low inflation is stretching paychecks further. Throw in Niño's gift of a mild winter in the East, and you have the makings of a powerful spurt in consumer spending and homebuilding. But at the same time, the Asian meltdown is hurting exports, and U.S. manufacturers are starting to feel the effects.

According to the latest data, not only were January and February retail sales vibrant, but overall prices of consumer goods are falling, meaning sales volume is surging. Housing starts boomed in February (chart), and in March, homebuilders said market conditions were the best in years. Also in March, first-time jobless claims fell to the lowest level of the year, suggesting continued strength in job creation and income growth.

SPENDING STARTS: BEST IN A DECADE?



Not only did retail sales not grow at all in January, perhaps a signal that businesses are making some downward adjustments to their stockpiles.

The bottom line: Domestic buying power, with its fast growth, is going to triumph in the first quarter. Growth in real gross domestic product is adding up to an annual rate of more than 3%—close to the 3.5% pace in the second half of last year. For the second quarter, a slowdown in domestic demand is likely, given that good weather and some spring-quarter buying to be brought forward into the winter. But with consumer fundamentals so strong, households may not stay out of action for long.

SISTENT STRENGTH in household demand has been the economy's key feature of the past year. It is as though—when all the first-quarter data are in—real consumer outlays for goods, services, and new housing will have accounted for more than 80% of the

economy's growth since the end of 1996. But the pattern has been a zigzag, with alternating quarters of spending sprees followed by respites.

The first quarter is clearly one of those sprees. Retail sales rose a healthy 0.5% in February, and January receipts jumped 1%, a gain that was revised sharply higher from the 0.1% increase originally reported. February receipts, which are based on only partial-month reporting, are likely to be revised upward as well, given the month's unusually warm weather and the strong weekly results of private-sector surveys.

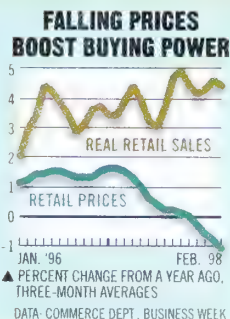
Leading the February sales gain: Department stores and clothiers each posted 1.3% increases in receipts, on top of advances of more than 2% each in January. Building supply and hardware stores also scored big gains, reflecting the boomlet in housing. Furniture store sales dipped 0.4% in February, but that followed the largest two-month gain in four years.

MOREOVER, WHEN RETAIL SALES are adjusted for inflation and to exclude those categories that do not enter the Commerce Dept.'s measure of real consumer spending in the GDP data, so-called core retail sales are on track to post the strongest quarterly advance of this seven-year expansion. A conservative estimate of first-quarter growth in real consumer outlays would be around 5%—which is about the same powerful pace at which real aftertax income appears to be growing.

Store receipts actually understate the volume of goods consumers are buying (chart). Average sales during the past three months are up only 3.4% from the same three months a year ago. But because overall retail prices have fallen 1.1%, the real volume of sales is up a much stronger 4.5%.

Of course, that price decline is exaggerated by the nearly 7% drop in prices at gasoline stations and by the more than 32% plunge in prices of computers and software. The fact is, excluding those two categories, prices for 90% of retail goods are rising 1.1%. That's slower than the 1.8% trend of price growth during the previous two years, but the deflation suggested by the overall index is far from a general trend.

Not only are consumers spending their income, but



they also have enough left over to relieve some of their debt burdens. Late payments on bank credit cards in the fourth quarter of 1997 dropped to the lowest level since 1994, says the American Bankers Assn. The percentage of accounts delinquent 30 days or more fell to 3.04%, down from 3.53% in the third quarter and from a record 3.72% a year ago.

CONSUMERS ARE ALSO SHELLING OUT for new homes. Homebuilders broke ground on new houses at an annual rate of 1.64 million in February, up a steep 6% from January. Regionally, the month's gains followed El Niño, with double-digit increases of 14.3% in the Northeast and 10.9% in the South. Midwest starts rose 8.1%, but building in the West dropped 7.9%, probably reflecting El Niño's unfriendly side.

Starts are likely to fall from the February peak in coming months, indicating in part the payback from the weather-related strength. But housing activity should remain at a relatively high level this spring and summer because of low mortgage rates, record-low inventories of unsold new homes, and generally solid consumer fundamentals. The National Association of Home Builders' latest index of market conditions dipped to 67 in March, from 68 in February, but February's results were the most upbeat in four years.

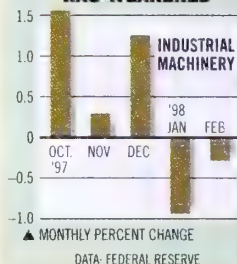
To be sure, the news on the first quarter is not all good, as the crosscurrents in overall demand begin to

hit manufacturers, who export a record 27% of the output. Earlier signs of weaker export orders and flattening out of overall nonaircraft bookings are now showing up in factory output. Industrial production, factories, utilities, and mines failed to rise in February as did output in the manufacturing sector alone.

Output does not appear to be collapsing, mind you. Factory production is on track to rise at an annual rate of about 3.5% this quarter, but that would be a considerable slowdown from the fourth quarter's 8% rate of growth. A chief weak spot recently is output of industrial equipment, which fell 0.3% in February, after dropping 1% in January (chart). Exports of capital goods make up more than half of all foreign demand for U.S. goods, and that is where Asian cutbacks have been the sharpest.

So if you're looking for a slowdown in the U.S. economy, the lesson from the first quarter is: Don't waste your time staring across the Pacific. Keep your eyes peeled on the labor markets, consumer spending, and business investment. If the slowdown is real, that's where it will show up.

EQUIPMENT OUTPUT HAS WEAKENED



CANADA

A BRAUNY ECONOMY IS TAMING THE BUDGET

The best news coming from Canada's fiscal front is about... nothing.

That at least is one way to read Finance Minister Paul Martin's announcement that the federal budget will be in balance for the fiscal year ending Mar. 31. Martin also said the balance will be zero for the next two years—quite a turnaround from Canada's huge deficits in the early 1990s (chart).

Spending cuts have helped to trim the deficit, but the real catalyst has been the robust economic growth that is lifting revenues in this heavily taxed country. Despite the Asian crisis and two major strikes, real gross domestic prod-

uct rose at a 3% annual rate in the fourth quarter. Real GDP grew 4.2% for all of 1997, the best pace in three years.

And the economy still shows some energy now, even with Montreal's ice storms, continued fallout from Asia, and tightening monetary policy. February payrolls rose by a large 81,700, while the jobless rate fell to 8.6% from 8.9%. The economy's vigor is why private analysts say that Ottawa will actually post surplus-

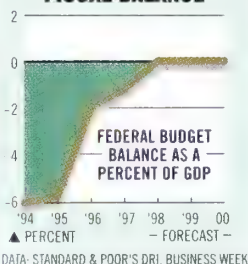
es this fiscal year and beyond. Martin's restrained forecast, however, is an attempt to head off a fight over how to spend any windfall. The conservative Reform Party wants some tax relief and

debt reduction. Even with its recent deficit-cutting, Canada's public debt stands at a massive 68.1% of GDP. The New Democrats want a rise in social-service spending. Martin's governing Liberal Party has pledged tax cuts for lower-income households, some increased spending, and—if there is extra cash—a little debt reduction.

In particular, Martin, who is seen as a possible successor to Prime Minister Jean Chrétien, has proposed federal scholarships for college students. But critics argue that the money should go directly to the provinces to improve Canada's universities. Clearly, the debate will heat up later on as the strong economy brings in more revenues. But Canada's politicians know that arguing over a surplus is far easier than cutting a deficit.

With Joseph Weber in Toronto

CANADA HEADS TOWARD FISCAL BALANCE





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LIVING IN A WORLD OF

Ultra-low prices are a boon for business—and just about everybody

Consider it a surprise birthday gift to the economy as the 1990s expansion enters its eighth year. Over the last six months the price of crude oil has plunged from \$22 a barrel to a low of \$12.91 a barrel on Mar. 17, a level not seen since October, 1988. And the prices of gasoline, electricity, and anything else produced with petroleum are headed down: Energy prices nationwide fell 2.4% in the first month of this year and are down 1% in the 12 months ended in January. In some cities, gasoline has fallen below 80¢ a gallon.

This year's stunning and unexpected decline in energy costs is causing cor-

porate planners to rip up their budgets. At current prices, Continental Airlines could save up to \$140 million on jet fuel this year, American Airlines says it spent \$50 million less in the first quarter alone, and Tenneco expects to spend \$4 less a ton to produce container board—and these cost declines drop straight to the bottom line.

What's more, the falling energy costs provide fuel for more economic growth. Because consumers are spending less on fuel and heating, they have more money to spend on other goods such as food, entertainment, and cars. And with falling energy costs holding down inflation, the Fed has another reason not to apply the brakes with interest-rate hikes. "This almost offsets the effects of the Asian crisis on U.S. economic growth," says David A. Wyss, chief economist at consultants Standard & Poor's DRI. Indeed, falling oil prices could add four-tenths of a percentage point to growth in 1998.

To be sure, oil prices could pop back up again. The biggest dangers are political disruptions of the oil supply—

most likely surrounding the situation in Iraq—or a sudden agreement among suppliers to cut production. Venezuela sent oil prices up a tick on Mar. 18 from their lows when it announced that it will attend OPEC's Mar. 30 meeting. That leaves some oil consumers waiting, hopefully—to see if the low prices stick. "If this continues for more than several months, we'd probably get more excited," says Continental Chief Financial Officer Lawrence W. Kellner.

But even skeptics accept that oil has moved into a lower trading range. For example, in January, when oil fell below \$17, Nizam Sharief, director of research at energy risk managers Hornsby & Co., predicted that crude would quickly return to a trading range of \$17 to \$21 a barrel. But Sharief—indeed many oil analysts—now see more forces holding prices down, to \$10 to \$15 a barrel even after this mild, El Niño-driven winter turns to a hot summer. Oil consultants Purvin & Gertz Inc. say it won't be until 2000 before oil averages \$17 again.

Why? It looks more likely Asia will



WITH GAS PRICES
LOW, CONSUMERS
CAN SPEND MORE
CASH ELSEWHERE

HEAP OIL

years to resume its prior growth and appetite for oil. Giant oil discoveries in the Caspian Sea region, off West Africa, and in the Gulf of Mexico's deep waters promise new sources of non-OPEC oil (page 54). Finally, the Organization of Petroleum Exporting Countries no longer has the ability to control pumping by its members. Most important, oil now is easier to find and retrieve, thanks to exploration and production technologies such as directional drilling. "There is chronic undercapacity for as far as we can see—up to 2005," says Leo P. Drollas, deputy director at the Centre for Global Energy Studies, a Houston-based oil watchers' group. Corporate budgeters are plugging those numbers into their spreadsheets, they see the glimmer of a new dawn. Big oil manufacturers are betting that raw materi-

als used in everything from plastics to drugs will fall 1.3% this year—the first time all decade. In the past 12 months, jet fuel prices are off 27%. And, in real terms, the \$1 a gallon U.S. consumers pay on average for gas is the lowest price in recorded history, according to the American Petroleum Institute.

"We're just beginning to assess what this will do," says Jerry Lowe, a vice-president and general manager at Tenneco Packaging. Beyond the savings in

its container-board manufacturing, Lowe sees oil savings augmented by electric deregulation. Tenneco, which now generates half the power to run its paper mills, is considering reducing its energy assets. "We want to make money in products, not energy plants," says Lowe.

Of course, falling prices affect industries differently. Oil companies such as Amerada Hess, Murphy Oil, and Unocal are reducing spending in anticipation of lower profits. Shares of the major oil-field service companies have tumbled, taking down the Standard & Poor's well equipment and services index 23% since Nov. 5. Small carmakers aren't seeing any benefit, either. "When you can buy a gallon of gas for less than it costs to buy a liter of bottled water, there aren't a lot of natural incentives to buy a small car," says Donald W. Hudler, president of General Motor's Saturn Corp.

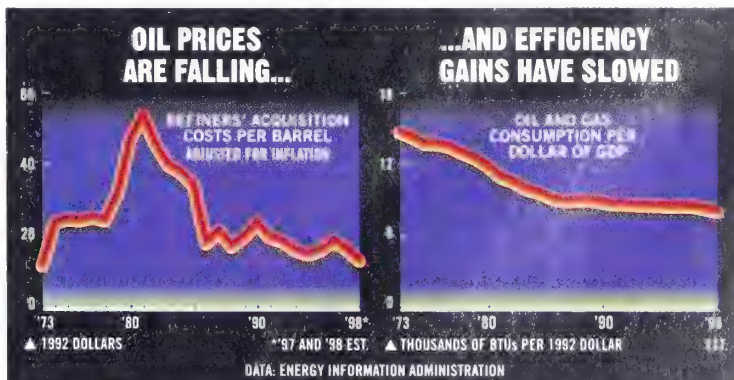
"MINI-TAX CUT." On the other hand, Detroit is selling lots of gas-hungry trucks and sport-utility vehicles. Falling gasoline prices "represent a minitax cut for consumers and provide our buyers with extra resources" to spend on their vehicles, says Ford Motor Co. senior economist Ellen Hughes-Cromwick.

Businesses could see a double payoff by continuing to push for energy efficiency. Unlike consumers, who can be expected to drive their Ford Expeditions more this summer, corporations have regulatory reasons to continue efficiency efforts. And many are able to chop manufacturing and processing costs while reducing energy demands. "There seems to be a sense it's energy's time," says Charles L. Watkins, president of Duke Energy's retail-services business. "The first thing I'm asked is, 'how can you save me 20%?' There's an assumption that prices will be falling."

Most oil companies seem to understand the new realities of the marketplace. Even at \$15 a barrel, oil companies can thrive, thanks to years of cost-cutting. "We've structured ourselves to exist in that type of an environment," says Phillips Petroleum Co. chief economist Alan H. Struth.

Now, other businesses are beginning to wake up to what the oil companies already knew. Barring political upheavals, crude prices seem likely to stay low—and that's good news for corporations and the U.S. economy.

By Gary McWilliams in Houston, with bureau reports



By Peter Coy

POLLUTION: TECHNOLOGY GOT US INTO THIS...

Cheap oil may be a sweet dream for owners of Chevy Suburbans, but it's a nightmare for environmentalists and others who are fretting about air pollution and global warming. Cheaper gasoline and other transportation fuels will lead to more consumption and more harmful emissions. "We have a dangerous period here for the environment," says David M. Nemtzw, president of the Alliance to Save Energy. "Cheaper oil is going to make it that much harder for the U.S. and other countries to reverse their course and get on to a more energy-efficient future."

What's worse, the standard prescription from economists—higher fuel taxes, to encourage efficiency—is politically Nowheresville. Sure, higher levies could be offset with reductions in other taxes, as on income, so the overall burden would not rise. But let's be realistic: Regardless of the merits, \$2 or \$3 gasoline would go over in Congress these days like a lead balloon.

Does that mean cheap oil is destined to poison the earth? Not necessarily. There is a potential fix that most politicians—and economists as well—have underestimated. It's technology. Revolutionary advances in finding and producing oil cheaply are largely responsible for increasing the pollution threat. Now it's time for another set of technologies to curb the pollution, by improving the efficiency with which society uses oil.

CLEAN MACHINES. The predominant use of oil is in transportation, particularly automobiles. So that's where the bulk of research and development on oil-consumption efficiency should be focused. All the world's auto makers are hot on the trail of "hypercars" that could get three times the fuel efficiency of today's average vehicles.

It may seem hard to believe that we're on the way to cleaner, more



CLEANING UP Just as it has created the problem by making oil abundant, science can cut our use of it

fuel-efficient vehicles, given the booming sales of large gas-guzzlers. Last year, the average fuel efficiency of cars and light trucks on U.S. roads declined for the first time since the 1970s. And the alternative vehicles on the road today are a sorry lot. General Motors Corp. has managed to lease only about 300 of its EV-1 electric vehicles despite a heavy subsidy.

But it's time to stop being jaded about alternative vehicles. In the past few years, laboratories in North America, Europe, and Japan have made major breakthroughs in clean, highly efficient diesel engines and in fuel cells, which extract energy from

hydrocarbon fuels without combustion. Suddenly, alternative vehicles aren't just for public relations anymore. In late 1997, Toyota Motor Corp. unveiled its Prius, a car that gets 66 miles per gallon from a hybrid power source consisting of batteries and a small gasoline engine. Ford Motor Co. and Daimler Benz have said recently they will begin selling fuel-cell cars by 2004, and GM says it will have fuel-cell cars "production-ready" by then.

GREEN ISN'T ENOUGH. These vehicles won't be stripped-down econoboxes that appeal to environmentalist do-gooders. If they are, they won't stand a chance in the marketplace, even with heavy government subsidies. The Clinton Administration is prepared to pony up money—in the form of tax breaks of up to \$4,000 per car—to jump-start mass production of alternative vehicles. But it's also pumping money into R&D, recognizing the need for hypercars that have all the range, power, and comforts of the best conventional cars of today. "You need a car that people will buy because it's better, not because it saves on fuel," says Amory Lovins, director of the Rocky Mountain Institute, a Colorado-based energy-efficiency outfit.

Western industrialized countries led by the U.S. are the world's biggest producers of greenhouse gases. Fortunately, they also have the wherewithal to do something about them. No question, today's low fuel prices create a formidable speed bump on the road to energy-efficient technologies. But that's no reason to give up the journey altogether. If coming technologies like fuel cells are as good as they're cracked up to be, eventually they will win in open competition for consumers' dollars. We had better hope so, anyway. Because there is no politically realistic alternative.

Coy is associate economics editor.

WHEN BOSSES GET RICH FROM SELLING THE COMPANY

Golden parachutes are rewarding dealmaking CEOs

When a company announces big merger plans, rank and file employees often suffer a mass anxiety attack. What plants will close? Which departments will shrink? Who will be laid off? In the executive suite, however, the mood is more upbeat. As this year's proxies show, when companies merge or sell out, executives get mindblowing deals whether they stay or ride off into the sunset—regardless of performance.

The payouts are big, in fact, and some observers are raising questions about CEO motives. Rich exit packages—so-called golden parachutes—are designed to relieve executives from having to worry about what could happen to them, so they could evaluate deals effectively," says Carol Bowie, research director of Executive Compensation Advisory Services, a consulting firm in Springfield, Va. "We've now moved 180 degrees, to the point that the issue is so big that it must be difficult, if not impossible, not to consider one's situation."

Charges of conflicts of interest are already surfacing. As part of its never-ending defense, Computer Sciences Corp. filed suit against Computer Associates International Inc., alleging that CEO, Charles B. Wang, tried to win CEO Van B. Honeycutt's support for a deal with a \$35 million payout and an employment contract worth \$17.5 million. CA denies the allegations.

PERFORMANCE ANXIETY. Even without such potential conflicts, the severance packages are eye-popping. Some million in cash, stock, and various options went to ITT Corp. CEO Rand V. Araskog when ITT was acquired by Starwood Hotels & Resorts. Although Araskog has left the company, in January he received an option grant of 100 shares of Starwood in exchange for help during the transition. The deal commits ITT to paying the "gross" taxes due on Araskog's cash severance payments. That could cost an additional \$22.5 million, says Donald R. Hirsch, principal at Pasadena (Calif.) Compensation Resource Group

Inc. And the package is unrelated to ITT's performance: Before its takeover battles began, ITT's stock had seriously underperformed the market.

Another sweet sendoff goes to Kent Kresa, CEO of Northrop Grumman Corp., who will collect a cash payment of \$7.8 million and see his stock rights and options worth \$16.1 million vest should Northrop's merger with Lockheed Martin Corp. go through.

Former Tandem Computers Inc. CEO Roel Pieper was another winner: After selling out to Compaq Computer Corp.

last year, Pieper walked away with \$6 million in cash, along with 650,000 new Compaq options and the conversion of Tandem options into Compaq ones. Tandem's earnings and stock price had languished for years before the deal.

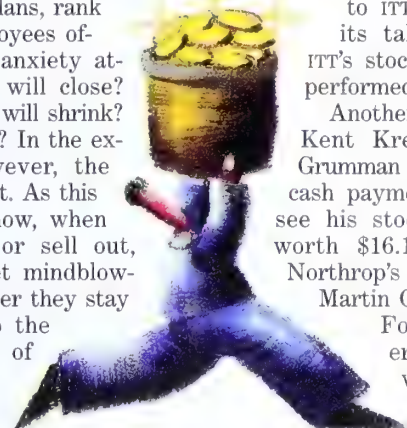
You don't have to leave to cash in, either. Sometimes CEOs who stay on get special bonuses as well. When Charles E. Rice, CEO of Barnett Banks Inc., sold

out to NationsBank Corp. last year and agreed to become nonexecutive chairman, he received 250,000 NationsBank shares and options for 400,000 more. The proxy stipulates that his annual salary and bonus must be at least \$3.5 million—and never less than that of NationsBank CEO Hugh L. McColl Jr. "That would appear to be an ego clause," says Charles M. Elson, a pay expert and professor at Stetson University College of Law. In 1996, Rice's salary and bonus totaled \$2.5 million.

RETAINER FEES. Then there's Bert C. Roberts Jr., chairman of MCI Communications Corp., which is being acquired by WorldCom Inc. If the deal goes through, Roberts will become chairman, and he and other senior execs will split a "retention-bonus pool" of \$170 million. Roberts' share: \$10.5 million. The move wasn't WorldCom CEO Bernard J. Ebbers' idea. MCI had negotiated similar terms in its failed merger with British Telecommunications PLC and extended the terms with WorldCom. "Basically, we walked into the BT-MCI agreement," says a WorldCom spokeswoman.

Another growing trend is to guarantee a departing exec a fat consulting contract. Northrop Grumman's Kresa, for example, would garner \$1.4 million in his first year as a consultant. IBM's latest proxy provides CEO Louis V. Gerstner Jr. a 10-year consulting contract upon retirement. He will be paid at the daily rate of his final salary.

But ex-executives don't even have to come



The Sweet Hereafter



ARASKOG



PIEPER



KRESA



ROBERTS



RICE

TAKE THE MONEY AND RUN

RAND ARASKOG	ITT by Starwood Lodging	\$20 million cash and stock, 162,500 new Starwood options
ROEL PIEPER	Tandem by Compaq	\$6 million, 650,000 new Compaq options
KENT KRESA	Northrop Grumman by Lockheed Martin	\$7.8 million cash

TAKE THE MONEY AND STAY

BERT ROBERTS	MCI by WorldCom	\$10.5 million cash bonus
CHARLES RICE	Barnett Banks by NationsBank	250,000 shares, 400,000 options; min. annual salary and bonus: \$3.5 million

DATA: COMPANY REPORTS, BUSINESS WEEK

back if trouble hits. After agreeing to merge Union Pacific Corp. with Southern Pacific Rail Corp. last year, then-CEO Drew Lewis got a \$4 million bonus along with a five-year, \$3.75 million consulting deal. The merger has been a disaster, snarling rail traffic across much of the country. So is Lewis now helping to get UP out of this mess? UP

spokesman Gary F. Schuster says he has been working on an "as needed" basis. "It doesn't matter if he works at all or a lot," says Schuster. "That's the deal the board cut with him."

With stocks in the Standard & Poor's 500-stock index up 12% this year, there is little outcry over dealmakers' pay. That may change as pay-related pro-

posals come up in annual meetings, says Ann Yerger, director of research at the Council of Institutional Investors. "Pay issues are probably the No. 1 concern for our activist members," she says. By annual meeting season, many deal-related bonuses will be in the bank.

By Jennifer Reingold in New York with Brad Wolverton in Atlanta

STOCK OPTIONS: LOU TAKES A CUE FROM SILICON VALLEY

Louis V. Gerstner Jr. is not yet in the same league as high-tech billionaires such as William H. Gates III and Lawrence J. Ellison. But the IBM CEO doesn't lack for incentive pay. His 1997 salary and bonus was \$6 million, up 26% from a year ago. What's more, he stands to

In a break from Big Blue tradition, he's opening stock-option programs to a wider group of employees—namely nonexecutives. Even though stock options for the rank and file have long been standard at other high-tech companies, IBM has typically granted options only to a small

performance-related bonuses by 30%, to \$1.3 billion. Meanwhile, the merit-pay pool is getting an extra \$2 billion.

The big motivator, though, is stock. This year, IBM will more than triple the number of employees who get stock options. That's on top of a 100% increase in 1997. "This is a great way to help bring the best people to IBM," says Josephine Tsao, the company's head of executive compensation.

HEFTY INCENTIVES. IBM is starting to catch up, but it is still lagging behind most high-tech companies. The average tech concern distributes about 3.3% of its stock in the form of employee options each year, according to Mark Edwards, a consultant with compensation specialist iQuantic Inc. This year, IBM is planning to set aside 2.5% of its outstanding shares for employees, up from 1.8% in 1997.

Gerstner's inner circle is also receiving more generous packages. In addition to salary and bonus raises of up to 31%, Gerstner is giving out hefty incentives in the form of restricted stock—essentially shares executives can cash in after a certain period for the full value. It's a much better deal than options, which increase in value only when they exceed a preset price. According to the proxy, IBM's top three executives received \$2 million worth of restricted stock each in 1997. "That's great for retention, but it doesn't do much for performance," says West.

So far, it's too early to tell if Gerstner's compensation scheme is working. But, says recruiter Jeffrey E. Christian of Christian & Timbers Inc., IBM isn't the recruiting paradise "it once was." And it won't be as long as Big Blue's stock keeps heading north.

By Ira Sager in New York



In the past, IBM gave options only to a small group—making it an easy mark for high-tech companies who came wooing managers

make a bundle on the 2.2 million shares he received as part of his annual compensation. According to IBM's proxy statement, Gerstner's stock could have a value of \$130 million if the share price appreciates at 5% annually for the 10-year option period. At a 10% annual increase, Gerstner's windfall swells to a cool \$1.3 billion.

Now, Gerstner wants more IBMers to get Silicon Valley-style rewards.

That makes IBMers an easy mark for other high-tech companies that come wooing. "They have lost a lot of people over the years," says Andrew W. West, whose San Francisco consulting firm, WardWest Pay Strategies, designs stock plans for high-tech companies. "They seeded the companies in the Valley."

To halt the brain drain, Gerstner in 1998 is sweetening the pot for

WELL, STEVE, WHAT'LL IT BE?

Apple's board may soon force Jobs to decide his role



be or not to be CEO? That is the question Steve Jobs can't seem to answer. Now, after months of waffling, it may be decision time. At a March board meeting, BUSINESS WEEK has learned, some Apple Computer Inc. directors plan to put the question to the founder and CEO pro-tem since last summer: Are you staying on permanently, or will you go and make way for somebody new? To encourage him to leave, insiders say, the company has offered Jobs a huge pay package—as much as 8% of the company.

But the offer can't sit on the table forever. Says one insider: "Some members of the board don't want to leave the ends open for eons." In fact, the company has identified a suitable replacement—who is only waiting for Jobs to make up his mind, insiders say. But that deal won't take the post unless Jobs is willing to give up the CEO title and ultimately the chairmanship as well. Other board members have said the same thing. "If I'm going to go there, I want to run the company," says one tech-industry veteran who has been considered for the post. "I'm not inter-

ested in being a utility infielder." Asked to comment on the situation laid out by insiders, Jobs told BUSINESS WEEK in an E-mail: "Your sources are wrong."

What is not in dispute, however, is Jobs's indecision. Last October, it seemed that he was ready to go. Returning from a soul-searching vacation in Hawaii, he told the board he would not take the top job permanently. Instead, he preferred to pursue his movie-mogul career as CEO of *Toy Story* creator Pixar Animation Studios and spend more time with his family. Weeks later, in December, he turned around and asked the board to make him an offer, according to insiders. The reason: With Apple showing signs of recovery, he figured he could juggle duties at Apple and Pixar.

Two days later, the board responded. Not enough, Jobs said. So the board sweetened

its offer and then waited. And waited. "We make him an offer, and it's like he took a two-month vacation," gripes one insider. Then, in a conference call with the board several weeks ago, Jobs suddenly asked again for the board's best offer. The result was the sweetest deal yet: 5% to 8% of Apple stock, worth up to \$270 million at today's price. According to insiders, Jobs still isn't sure.

Indeed, the Apple founder's zigzagging has directors worried about how long he might stay if he does accept. "When a guy vacillates for this long, it tells you a lot," says one insider, who figures Jobs will go by yearend. "After all the chaos Apple has been through, the last thing it needs is a permanent CEO for six months." As insurance, three of the six members on Jobs's handpicked board are pushing to hire a strong No. 2, company insiders say.

HELLO, COLUMBUS? Is Jobs good for Apple? He certainly has been. After years of muddy decision-making by predecessors, Jobs has simplified Apple's Macintosh product line, streamlined its distribution, and killed poor-selling products like the Newton. New products unveiled on Mar. 17, including a Mac that is claimed to be faster than any Pentium PC and a sub-\$1,000 consumer model expected out in coming months, could drive sales through the rest of the year.

FENCE-SITTING: J. P. Morgan Securities analyst Daniel Kunstler expects Apple to earn \$155 million on sales of just over \$6 billion for the year.

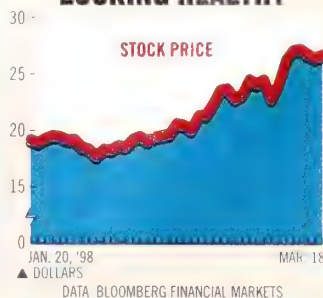
That has made Apple's stock a sizzler—more than doubling, to 26, since January. Says former Chief Financial Officer Joseph Graziano: "Steve has made a lot of tough decisions that [former CEOs Michael Spindler and Gil Amelio] weren't willing to make."

The problem is that Apple's recovery could well be short-lived, and insiders say that Jobs would not like to preside over a dying Apple. But the situation isn't hopeless. Apple is preparing products to extend its brand into new mar-

kets, including a TV set-top box-cum-Mac, dubbed Columbus. But with Mac market share down to low single digits, the safer decision may be to stick to the movie business: Thanks to a recent runup in Pixar's stock, to more than \$33, Jobs's 72% stake is now worth \$1 billion.

By Peter Burrows
in San Mateo, Calif.

APPLE'S STOCK: LOOKING HEALTHY



COMMENTARY

By Suzanne Woolley & Paula Dwyer

MARKET OF THE FUTURE? DON'T HOLD YOUR BREATH

At first blush, the proposed merger of the NASDAQ Stock Market and the American Stock Exchange seems like welcome news for investors. By creating a more formidable rival to the New York Stock Exchange, the linkage of the NASDAQ and the Amex could lead to more efficient markets. Combining the auction system of Amex and NASDAQ's dealer system could yield a hybrid electron-

now use the computerized system when they want to and avoid it when they don't. "London is run in many ways for the benefit of the professional trading firm," says Columbia University law professor John C. Coffee Jr., who is on NASD's legal-advisory board.

Most attempts to change U.S. markets have also failed. InterVest Financial Services, for example, was

ed, and that their jobs won't disappear. That's not progress. "Floor brokers are a 19th century Dickensian institution that still survives in an era of electronics," says Columbia's Coffee.

There are other innovations in the works—changes that also must overcome the human factor. For example, NASDAQ is proposing an electronic system developed by OptiMark Tech-

BYE-BYE, FLOOR BROKERS?

Not likely. To get the deal with NASDAQ done, Amex promised the brokers their jobs would not disappear

ic-auction market that would present new choices and potential cost savings for issuers, traders, and investors. "It's the catalyst that will lead to a complete reengineering of our markets," says Junius W. Peake, a professor at the University of Northern Colorado and a former National Association of Securities Dealers director.

Don't count on it. Introducing structural changes at the exchanges has often been an exercise in futility. Such efforts inevitably hurt the financial interests of entrenched Wall Street firms and trading-floor personnel by reducing their role as middlemen. If a new trading system does develop, as it has in London, the original design is likely to be watered down to make it palatable to vested interests—at the expense of creating a more liquid, open market that would benefit all investors.

Consider the tale of innovation interrupted at the London Stock Exchange. For years, the LSE had used market makers, as NASDAQ does. Then, in 1996, exchange officers at the LSE proposed creating a computerized auction system that would match buy and sell orders and be more efficient for investors. But once market makers realized that the system could deprive them of business, they, as owners of the exchange, voted out their CEO. Market makers

created as a trading system for the secondary bond market, which has no central posting of bids and offers. InterVest would post bids and offers electronically, allow instant execution, and give traders anonymity. The goal was a cheaper, more efficient market. But InterVest's founder says bond dealers refused to use the service since it usurped their role. InterVest is now trying to become an Internet-based system but has run out of money.

"DICKENSIAN." Proponents of the NASDAQ-Amex deal, which was approved by both boards on Mar. 18 and now awaits a vote by Amex members, say that it will merge the best elements of dealer and auction markets. But already that vision is getting blurred by politics. To get the deal done, Amex must convince floor brokers that they aren't voting themselves out of existence. So far, the brokers have been assured that the trading floor will remain for 10 years, that a new floor may be creat-

nologies as an adjunct trading system. OptiMark uses artificial intelligence software to help institutional investors trade large blocks of shares without revealing their strategy or identity—something that's not possible in the NASDAQ market. "NASDAQ is starting to understand how to create market systems that investors want," says Harold Bradley, a fund manager with American Century Investment Management. But OptiMark undercuts the role played by block trading desks, so it faces high hurdles.

It's another reminder that the stock exchanges are still run for the benefit of their members and securities firms, not for companies and their shareholders. Until that situation changes, deals like the Amex-NASDAQ hookup won't produce the gains investors expect and deserve.

Woolley covers the markets in New York. Dwyer covers securities from Washington.



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COMMENTARY

By Howard Gleckman & Dean Foust

WHY CONGRESS CAN'T AFFORD TO SHATTER GLASS-STEAGALL

It's an election year, so it's time for biennial rituals. Lawmakers are cutting ribbons at senior citizen housing projects. They're touring local schools. And Congress is debating whether to overhaul the Depression-era law that kept banks, securities firms, and insurers out of each other's business.

When the dust settles this fall, two things will be certain: The 1933 Glass-Steagall Act will still be on the books. And the campaign coffers of Washington lawmakers will have been filled by financial-services firms, which forked out more than \$19 million in 1997 alone. "They are raising money from the competing industries big, big time," says one bank lobbyist.

This year, House Speaker Newt Gingrich (R-Ga.) is pushing for passage of a financial-services deregulation bill by Easter. It wouldn't do anything for banks, which have won approval by the courts and regulators to sell mutual funds, do some securities underwriting, and peddle insurance. Indeed, it would impose new restrictions on the ability of banks to sell insurance. But the bill, a compromise cobbled by Representative John A. Boehner (R-Ohio), would give brokers a boost, permitting them to acquire banks, which have the power to lend and take federally insured deposits.

FLOOD OF CASH. The bill's backers vow they will succeed at last. "I know it has failed 10 times in the past 20 years, but this time is different," says Bruce E. Thompson, Merrill Lynch & Co.'s chief lobbyist.

chance. The Clinton Treasury Dept. poses the bill. So do consumer groups. And banks, long advocates of Glass-Steagall reform,

now contest any change in an act that still limits the powers of brokers and insurers. Even if the bill clears the House, Senate Majority Leader Trent Lott (R-Miss.) has said he won't consider controversial legislation this year.

But the mere threat of a House

vote has unleashed a flood of campaign contributions from banks, insurers, and brokerage companies. In 1997, securities firms ponied up \$4.3 million, while insurers gave \$3.8 million and banks and other lenders gave \$1.8 million to the national Democratic and Republican parties. That was nearly 20% of all the unlimited soft-money donations the two parties got from Corporate America. It's the same with political action committees. Financial service PACs have given \$10 million so far in this election cycle—nearly double

the next most generous industry.

Boehner knows the fund-raising power of Glass-Steagall legislation well. In January, just before he brokered the GOP bill, he hosted a golf outing at California's Rancho La Quinta that attracted a gaggle of financial-services representatives. The price to tee off: \$1,500. Boehner has scheduled another golf fund-raiser for Jacksonville, Fla.

But the big bucks buy only stalemate on Capitol Hill. Elsewhere, court decisions and new technology such as electronic banking are rendering Glass-Steagall as obsolete as the Model T. Except, of course, when it comes to driving home those campaign contributions.

Gleckman and Foust have covered banking reform again, and again, and again.

SHAKING THE MONEY TREE

Banks, brokers, and insurance companies are among the most generous soft-money givers to both Democrats and Republicans

TOP EIGHT GIVERS:	MILLIONS
SECURITIES & INVESTMENT FIRMS	\$4.336
INSURANCE	3.841
TELECOMMUNICATIONS	3.521
REAL ESTATE	3.237
TOBACCO	3.070
OIL & GAS	3.040
ENTERTAINMENT & MEDIA	2.278
BANKS & LENDERS	1.791
TOTAL BUSINESS:	\$51.402

DATA: FEDERAL ELECTION COMMISSION, COMMON CAUSE



LAMPE-ONNERUD: Bellcore pioneer

TECHNOLOGY

BATTERY BREAKTHROUGH

Plastic power is on the way, and the U.S. leads the charge

Last September, at the World Expo in Tokyo, Japan's digerati got a glimpse of the world's thinnest notebook computer. Built by Mitsubishi Electric Corp., the Pedion measures just over half an inch thick and weighs only 3.1 pounds. The secret: a revolutionary new type of lithium battery made from flexible sheets of plastic. But the biggest surprise was the battery's pedigree. It didn't come from Sony, Sanyo, or Toshiba, whose batteries power most of the world's portable computers. It was made by a Newark (N.Y.)-based startup called Ultralife Batteries Inc.

Ultralife is part of a new gang of U.S. battery makers that see their future in plastic. And all of them are targeting the booming market for portable electronics gear. In 1997, manufacturers around the world shipped some 14.7 million mobile computers, along with nearly 90 million cell phones, according to Dataquest. By 2001, yearly notebook sales could reach almost 30 million units, and phone sales could exceed 210 million. Users will expect improved performance, says Dataquest analyst Mike McGuire. "Everyone is interested in seeing new battery technology."

All the U.S. developers of plastic lithium batteries have licensed key tech-

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nology from Bellcore, the former research arm of the Baby Bells, which unveiled the world's first workable designs back in 1993. Instead of compressing liquid chemicals in a metal tube, Bellcore scientists encapsulated them in plastic. So the batteries are safe and can be folded to fit any product shape. "That affords design freedom that no other battery provides," says Andrew J. Zaremba, product line manager at Hewlett-Packard Co.'s mobile-computing division. And now that the technology is widely dispersed, "we will finally start to see a lot more product in the market," says Christina Lampe-Onnerud, Bellcore's senior scientist in charge of battery development.

AUTOMATION SNAG. Once a few kinks are ironed out, that is. As Hewlett-Packard learned firsthand, plastic lithium batteries are easier to admire than to build. With help from Mitsubishi, HP on Mar. 18 unveiled a U.S. version of the Pedion, called OmniBook Sojourn. But Ultralife, which had been hired to make plastic batteries for HP, hit a snag automating its production line. So instead, the Sojourn runs on a new lithium-ion design. These batteries are light and thin, but designers say they still would like plastic.

Ultralife isn't the only one to suffer production glitches. Over the past nine years, Valence Technology Inc. of Henderson, Nev., has invested \$150 million in developing plastic lithium batteries. But the company has been slow to get products out the door and doesn't expect volume shipments until the fall.

In the face of such delays, some large potential customers, including Compaq Computer Corp., remain skeptical about plastic batteries. Other than flexibility in design, says Ted H. Clark, Compaq's marketing vice-president in the portable-PC division, plastic "has few advantages over lithium-ion today." Shares of both Ultralife and Valence are trading far below their 52-week highs.

Another concern is mounting competition from Asia. The Japanese currently own the lithium-ion market and are feverishly pursuing plastic technology—from both Bellcore and domestic companies. Toshiba, Sony, and Matsushita could all, at some point, be major players. A Bellcore licensee in Malaysia called Shubila Battery is also ramping up production. But whether the game remains in the U.S. or moves to Asia, plastic batteries are on track to just keep going and going and going.

By N. Gross in New York, with Irene Kuntz in Tokyo and Nathan Estep in Fort Lauderdale, Fla.

COMMENTARY

By David Greising

IS BIG TOBACCO'S ANTISMOKING PUSH A SMOKESCREEN?

Some people might think that Big Tobacco was smoking something pretty strong when it offered to fund massive advertising to discourage underage smoking. They would be wrong.

Sure, the campaigns are aimed at scaring future smokers off. But Big Tobacco realizes that such efforts to brainwash rebellious teens are very likely to fail. They know, for example, that underage smokers mimic young adults, who can smoke legally beginning at age 18. When 14-year-olds see Leonardo DiCaprio lighting up on screen, millions spent on antismoking messages go up in smoke.

Small wonder, then, that in all the state lawsuits the industry has settled, it has expressly limited antitobacco programs to underage smokers. "The tobacco industry has done a great job of snookering everyone into saying, 'Just let's stop kids from smoking.' To the extent any program is limited to youth, it will fail," says Stanton A. Glantz, an antismoking activist.

To stack the deck further, when the industry settled in Florida, which kicks off the first statewide teen-antismoking campaign at the end of March, it limited the campaign to 24 months—not much time to change the attitude of an entire generation. Florida is seeking an extension.

Will anything stop teens from starting? Appeals aimed at getting in-the-moment youths to consider long-term



COOL, MAN

From Dean to DiCaprio, teens find smoking sexy in the movies

health risks are largely futile. Pocketbook arguments are ineffectual, too. In their early teens, young smokers consume relatively little—maybe a pack a week. So the price increase, unless it's sudden and massive, is an unlikely deterrent. As John P. Pierce, head of cancer prevention at the University of California at San Diego, points out, a proposed \$1.50 per pack federal tax would cost teens far less per week than they spend on one movie. "If kids were that price-sensitive, they'd all be smoking generics, but they're all smoking Marlboros," he says.

ANTI-AUTHORITY. Two main messages work with teens, according to a study of anti-smoking campaigns in California, Massachusetts, and other states by Glantz in this month's *Journal of the American Medical Assn.* Ads portraying the tobacco industry as deceitful and manipulative resonate with teens already inclined to suspect authority figures. And ads that focus on the dangers of secondhand smoke can arouse a sense of injustice.

Florida will test those themes, along with others, when it convenes a youth summit on Mar. 29. "A lot of states are looking to Florida," says Gary T. Rudman, president of marketing firm Teen-Age Research Unlimited. "There's a lot of pressure on them to do it right." And a pile of odds stacked against them.

Greising covers the tobacco industry for *BUSINESS WEEK*.

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MANAGING

STIRRING THINGS UP
AT QUAKER OATS

Will axing Gatorade's
Doyle and other top
execs help cure
its ills?



When James F. Doyle plopped down on a lobby sofa at the Naples (Fla.) Ritz-Carlton for a chat with his boss on the evening of Feb. 16, he had no idea he was about to be fired. The 45-year-old head of Gatorade had led the brand to six years of red-hot growth—even as parent company Quaker Oats Co. had struggled under the weight of its disastrous \$1.7 billion Snapple acquisition. Doyle and new Quaker CEO Robert S. Morrison had just finished rehearsing speeches they would give to Wall Street analysts the next day outlining Quaker's growth strategies.

But during a 20-minute chat, Morrison made it clear that Quaker's future and Doyle's would no longer converge. "It was new news to me," Doyle says. Morrison, who left the top job at Kraft Foods Inc. to join Quaker in October, told Doyle of his plan to eliminate an entire level of top management, including Doyle. On Mar. 12, Morrison announced those changes and promoted 10 managers to oversee Quaker's various brands, including Life cereal, Rice-A-Roni, and the flagship oatmeal line. All report directly to the CEO. Morrison also announced a \$1 billion stock buyback.

It's all in an effort to wake

the 97-year-old Chicago food company from the management torpor that Morrison says has held it back. With \$5 billion in annual sales, Quaker is a relatively small player in food—less than one-sixth the size of Kraft—but its organization is more convoluted. "We have an unnecessarily complex structure," Morrison told analysts Mar. 12, adding that the jobs he cut "are no longer needed [or] relevant."

MANAGEMENT ON A DIET

WHO'S OUT....

Three executive vice-presidents:

JAMES DOYLE, 45, Gatorade chief

BARBARA ALLEN, 45, head of international foods

DOUGLAS MILLS, 52, head of North American foods

...WHO'S IN

Nine line managers now reporting directly to CEO Robert Morrison, including:

BERNARDO WOLFSON, 44, Latin American businesses

CASSIAN CHEUNG, 42, Asian businesses

SUSAN WELLINGTON, 39, U.S. Gatorade

HARRY DENT, 40, cold cereals

CHARLES MANISCALCO, 44, snacks business

POLLY KAWALEK, 43, hot-cereals business

MARK SHAPIRO, 42, rice and pasta products

RUSSELL YOUNG, 49, manufacturing

TERRENCE MOHR, 54, sales

DATA: QUAKER OATS

Still, analysts mourn Doyle's departure. Doyle "was one of the few no-nonsense executives in a company where there was clearly a lot of nonsense," says Prudential Securities analyst John J. McMillin, referring to the Snapple debacle. Gatorade's 8% U.S. revenue growth in 1997, to \$1.2 billion, beat any established food brand, says Steven M. G. Braith, a Sanford C. Bernstein analyst **IN THE BAG**. With the new organization Morrison makes his mark—anointing a new cadre of mostly younger execs and purging those elevated by his predecessor, William D. Smithburg. Smithburg stepped down in 1997 after Snapple was sold for a \$1.4 billion loss. The division will no longer operate as separate food units, as Gatorade had under Doyle.

Morrison is also aiming to generate \$15 million in annual savings. The cuts are key because future revenue growth won't be easy for Quaker. Its hot-cereal business, which Prudential says accounts for 9% of revenue and 16% of earnings, isn't growing much. In cold cereals, sales grew 22% in 1997 as Quaker expanded distribution and introduced cheaper bagged products. But domestic sales can't expand forever, and bagged cereals have relatively low margins. Plus, Quaker is vulnerable to price cuts by bigger rivals such as General Mills Inc. Even Gatorade isn't without problems: It lost roughly \$15 million in the often slow fourth quarter.

Internationally, the situation is downright troublesome. Only 3% of Quaker's operating earnings come from overseas, even though 21% of revenues is international. Analysts say Morrison will likely trim and sell the European food business. Gatorade's Latin American business is strong, but it has struggled in Asia.

Will the changes work? At first, Wall Street was encouraged—bidding up Quaker's shares more than 5%, to as high as 60%. But by Mar. 18, the stock had retreated to 57%.

Meanwhile, Doyle is biding his time until a noncompete clause lets him back in the food business. He's taking a separation package he calls "more than fair" and heading off for the Caribbean and a weeklong family vacation on a 51-foot boat. You can guess what beverage they won't have on board.

*By David Leonhardt
in Chicago*



How to squeeze more "P" out of your P&L.

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EDITED BY PAT WECHSLER

THE LOCKHEED DEAL MAY COME UNDONE

IS LOCKHEED MARTIN'S \$11.6 billion bid for Northrop Grumman Corp. unraveling? At a meeting with government officials Mar. 16, the company offered to divest \$1 billion in defense electronics assets and agreed to let competitors bid for subcontracting work on items such as radar. That wasn't enough for the Justice Dept., which wants Lockheed to shed \$4 billion worth of Northrop Grumman's electronics business to make sure Lockheed-Martin doesn't favor in-house suppliers. For the company, that's a deal-breaker. The two sides were meeting to try to negotiate their differences but sources at Justice

say the antitrust division is prepared go to court to stop the deal if a compromise can't be reached.

CHASE WIELDS A BIG AX

IN ANOTHER BELT-TIGHTENING move for big banks, Chase Manhattan announced on Mar. 17 it would cut 6% of its workforce, or 4,500 employees. Savings from the cuts, estimated to be \$460 million, will be put into high-growth businesses such as investment banking and mortgage servicing. "I would call it better rationalization of scarce resources," says Hal Schroeder, of Keefe, Bruyette & Woods in New York, commenting on the layoffs. The company hopes to accomplish almost half of the cuts through attrition.

HEADLINER: ROBERT JOHNSON

A BIG BET ON BET

BET Holdings Chairman Robert Johnson may finally succeed in taking his company private. On Mar. 16, with the help of longtime partner Liberty Media, the cable impresario who founded the Black Entertainment TV network in 1980 offered shareholders a sweetened \$63 a share to take his company private—up from the \$48 he first offered in September. The deal, likely to go through this summer, will free Johnson to fund his expansion plans without worrying about the impact on earnings or the concerns of other shareholders. His



goal is to leverage BET's brand recognition among African-Americans in non-cable ventures such as magazines, clothing, and financial services. And its lucrative core cable business—which Acorn Fund manager Chuck McQuaid says will generate \$85 million in cash flow in fiscal 1998—is ready to foot the bill. In the future, look for some of these new businesses—such as the BET SoundStage Restaurants—to be spun off, says analyst H. Bernard Dorshow of Baltimore-based Chapman Co. *By Catherine Yang in Washington*

CLOSING BELL

CELLS RING

If you put your money in cellular stocks at the first of the year, you must feel very smart indeed. Local and regional wireless providers have become prime targets for big phone companies. The largest leap came on Mar. 13, when the cell index jumped 6.8%, to 275.8, on news that Alltel would buy 360 Degrees Communications. Cell stocks have jumped 75% since January, vs. 35% for the S&P. But Bear Stearns analyst David Freedman says we may have already seen the biggest jumps in the index.

COMPROMISING ON INTERNET TAXES

HOUSE REPUBLICANS ARE trying to avert a war between the states and the feds over Internet taxes. President Clinton backs a moratorium to help E-commerce take hold; states want the sales-tax revenue. The House may soon adopt a compromise. A bill to be introduced as early as Mar. 18 by Representative Chris Cox (R-Cal.) would pave the way for governors to impose levies after three years, half the moratorium proposed by the original bill backed by the industry. It will also establish a commission charged with setting ground rules for state sales taxes on Net commerce. The panel would have two years to finish its work.

off its back. On Mar. 17, the publisher agreed to sell its Dow Jones Markets unit, formerly known as Telerate, for \$510 million. The buyer, Bridge Information Systems, still must obtain financing. In its costliest acquisition ever, Dow Jones bought Telerate in the late 1980s for a steep \$1.6 billion. In late 1997, the company wrote down the value of its investment by \$992.5 million and now says it will take an additional write-off of unspecified size as it closes the books on the Telerate fiasco.

home detention for making illegal campaign donation. Stewart will cough up \$100,000, with the remainder to be paid by his \$1 billion privately owned company. Stewart admitted to funneling donations through his employees to various federal candidates. But his money, still good to the Republicans: Stewart has contributed \$20,000 this year and the state party says the funds will not be returned.

ET CETERA...

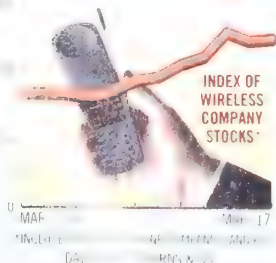
- Ad agency Wells BDDP closing after months of fighting and client defection
- Boeing was hit with an \$8 million suit charging the jet maker with racial bias.
- Dow Chemical is suing Union Pacific for losses allegedly from rail tie-ups
- Cement-maker Southdown is buying Medusa for about \$1 billion in stock.

CLOSING THE BOOKS ON A FIASCO

DOW JONES & CO. MAY FINALLY get the Telerate monkey

STEWART HIT WITH \$4.9 MILLION FINE

BUSINESSMAN THOMAS STEWART, owner of Seattle-based Food Services of America and the largest Republican contributor in Washington, agreed to pay a \$4.9 million fine and serve 60 days of





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EDITED BY OWEN ULLMANN

AN 'A DIFFERENT KIND OF DEMOCRAT' RETAKE THE HOUSE?

Shelley Berkley has the kind of business-friendly résumé that should make the local chamber of commerce ecstatic. The Las Vegas congressional candidate is a former president of the Nevada Hotel & Motel Assn., general counsel to local utility, and former deputy director of the Nevada Commerce Dept. She's also a Democrat. And she laughs at Republican attempts to paint her as a liberal: "That's a label I will be tough to stick on me."

With Democrats dreaming of recapturing the House this fall, Berkley is part of a crop of candidates out to moderate the party's reputation in the House as a bunch of left-wingers. The crew includes economic moderates, social conservatives, and unabashed business backers. "We're trying to recruit candidates who fit the districts," says Representative Martin Frost (ex.), head of the Democratic Congressional Campaign Committee.

TALK. That's pretty basic politics. Yet in the past, the Democrats leaned heavily on tri-tyers, friends of labor, and other liberal activists for their pool of House candidates. No more. Under Frost's four-year rule as chief recruiter, the party's Class of '96 turned out to be the most pro-business in memory. Frost says a comparable group of candidates will help Democrats capture the 12 seats needed to oust Newt Gingrich out of the Speaker's chair (table). While some say a takeover in '98 remains a long shot, the new class of recruits boosts the party's chances in key battlegrounds. "It takes a different kind of Democrat to even have a chance of winning" in some of the conservative districts targeted, says Joe Turnham, an Alabama social conservative trying to unseat Republican freshman Bob Riley. Turnham, the state Democratic Party chairman, is just a candidate. He helps run his family business—selling land for auditoriums, churches, and grandstands. A staunch

backer of civil rights and public schools, he's also in sync on social issues with Christian conservatives. "A lot of Democrats feel uncomfortable debating moral topics in the Christian community," he says. "I'll debate my opponent on the issues or do Bible sword drills."

In Pennsylvania, antiabortion candidate Patrick Casey, son of ex-Governor Robert P. Casey, gives the Democrats a good shot at winning a district long held by the GOP. Similarly, a pro-life, pro-gun gospel singer, Dave Phelps, is the best bet for holding a marginal Democratic seat in Illinois being vacated by the party's nominee for governor. These candidates have another advantage: money. In races with no incumbent, the 14 candidates with the biggest war chests are all Democrats.

Republicans aren't quaking at the sight of a few formidable foes. GOP strategists note that many of the strongest potential candidates have turned Frost down, and some conservatives may get knocked off in primaries by traditional liberals. Even if the newcomers win, the GOP won't go easy on them in the fall. "They've had people for 20 years who have claimed to be conservative while at the Rotary Club and then voted liberal in Washington," jabs National Republican Congressional Committee Chairman John Linder (R-Ga.).

The GOP also points out that a similar recruitment gambit by Senate Dems failed in '96. All eight centrist business executives tapped to retake the Senate lost their races.

The difference this time: Unlike those Senate "business-crats," who were neophyte candidates, Frost's friends all have at least some political experience. Besides, Frost has little choice but to seek out the center. If the Democrats are to have any hope of retaking the House, they have to go where the swing voters are.

By Richard S. Dunham

HOUSE OF REPRESENTATIVES

CURRENT MEMBERSHIP

Republican	227
Democrat	204
Independent	1
Vacancies	3

OPEN SEATS IN PLAY

Republican	12
Democrat	9

VULNERABLE INCUMBENTS

Republican	17
Democrat	10

Needed for majority 218

CAPITAL WRAPUP

FORMING SECURITIES REFORM

Congressional support is building for a bill making it tougher for investors to file class actions against public companies. The measure would amend a 1995 reform law that protects high-tech companies from suits if rosy forecasts turn out wrong and stock prices drop. Since enactment, investors have used a loophole—suing in state courts. The new bill would ban such actions. The Securities & Exchange Commission favors the change, but it wants lawmakers to

make another change in the '95 statute: setting a more lenient standard for fraud suits in federal court.

DR. NEWT BESTS DOC HILLARY

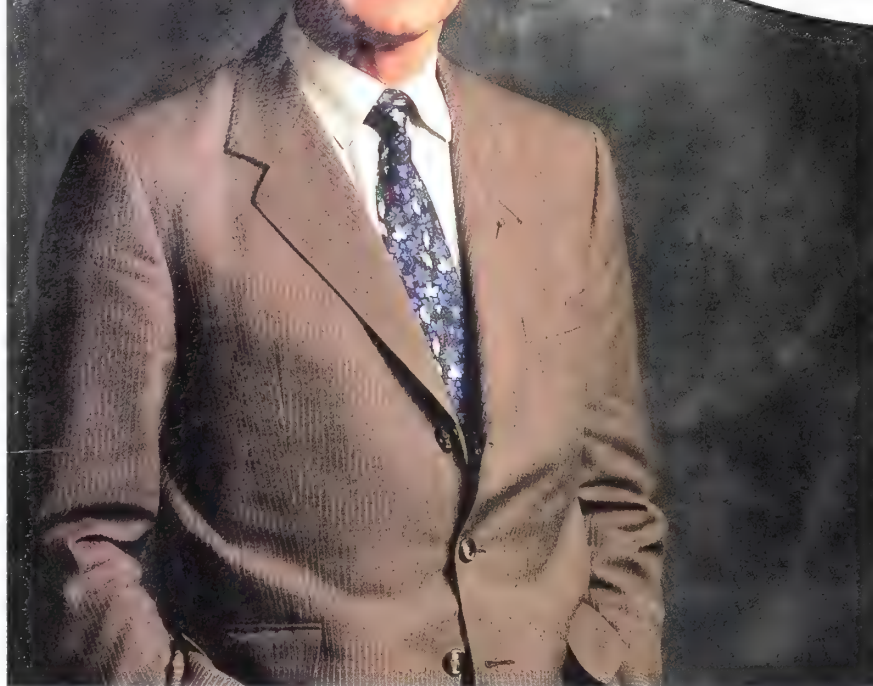
► Hillary Clinton still faces public suspicion about fixing medical-care problems. A suburban Washington focus group was assembled on Mar. 11 to help the American Heart Assn. and other health groups gauge public attitudes. Asked who they trusted to reform health care, the First Lady or House Speaker Newt Gingrich, a majority chose Gingrich.

CLINTON'S IMF STRATEGY

► With House conservatives vowing to slap antiabortion and other measures onto a bill giving the International Monetary Fund \$18 billion, the White House is now focusing its lobbying on the Senate, where IMF support is broader. The strategy: push for a quick Senate vote, and step up pressure on wavering House members. The plan made progress on Mar. 17, when a Senate panel approved funding—though with conditions the Administration hopes to water down.

- Purchase Rolls-Royce, which would crown Volkswagen as a gilt-edged brand
- Buy Scania, which would add heavy trucks to the product line
- Overtake Toyota as No. 3 vehicle manufacturer with across-the-board brand recognition
- Burnish the VW brand to match Mercedes-Benz
- Making RR efficient could cost the cars their exclusive image
- Global overcapacity and price wars limit VW's chances to
- VW could sacrifice quality standards, which are the key to catching Japan's leader
- Luxury-car buyers may balk at paying big for a VW

DATA: BUSINESS WEEK



GERMANY

IS VW REVVING TOO HIGH?

Piëch's grand plans could stall the carmaker's comeback

You would never pick Ferdinand Piëch for a dreamer. The pragmatic, 60-year-old chief executive has had Volkswagen in the repair shop for five years. Now that it's running again, however, Piëch plans to add a supercharger and lots of flashy chrome. To take VW into ultraluxury cars, he wants to buy Britain's Rolls-Royce. He hopes buying Scania, the Swedish truckmaker, will haul VW into the heavy end of the vehicle market. Piëch even entertains

plans for a V8-powered Volkswagen to compete directly with Mercedes-Benz. The goal: overtake Toyota Motor Corp. as the world's No. 3 carmaker.

Piëch's skills as a fixer are clear. A fleet of hot new models, including the stylish new Passat, has rocked rivals such as Adam Opel and Ford Motor Co. Profits continue to rebound from the heavy losses of the early 1990s, hitting \$748 million last year on sales of \$62.2 billion. In Europe, SEAT and Skoda, once-

weak subsidiaries, are growing briskly. Its luxury brand, Audi, is going strong. In the U.S., Beetlemania is powering a VW comeback. Even in Asia, VW sales have been barely dented by the economic crisis, thanks to its market leadership in China.

The risk in Piëch's dreams: He may push too far, too fast. VW still faces a host of problems. The launch of a new version of the best-selling Golf has been a disaster. Factories in western Germany rank among Europe's least efficient. VW's quality is middle-of-the-road. Management is overtaxed, and adding more tasks could short-circuit VW's turnaround. "They just don't have the human resources," worries an executive at a large institutional investor.

Nonetheless, Piëch envisions a grand future for the company his grandfather, Ferdinand Porsche, co-founded before World War II to build "the people's car." The iron-willed Piëch wants to distance VW from its mass-market heritage and mold a brand with a Mercedes-like reputation—and Mercedes-like margins. He has already set new industry standards for luxurious interiors in mid-market models such as the Passat and the Golf. Next, he plans to point new models squarely at Mercedes. One, informally called the Passat Plus, likely will make its debut in model year 2000. There's even talk of a top-end V12 model. But persuading consumers to pay Mercedes prices for a VW badge would be tough.

BIDDING WAR. Rolls-Royce would crowd the product range—if Piëch wins the bidding war against BMW and others. That could be clear within a few weeks. "When a brand like this is available, it's a one-time opportunity," says Robert Büchelhofer, VW's managing director for sales and marketing. And buying Scania would give VW a strong global presence in heavy trucks, a segment VW has explored only in Brazil. It's unclear, though, whether a deal can be struck. Scania officials say that they have discussed only joint projects.

With \$11 billion in cash and an im-

rights offering expected to raise \$300 million more, VW can afford a spree. But it comes up short, say former executives and others close to the company, in top management. Pointing to BMW's difficulty in digesting Rover Group Ltd., the sources warn that acquisitions can be distractions. That's particularly true in environments where VW has little experience. Analysts fear VW could ruin RR's exclusivity cachet in its effort to boost efficiency. VW still has repairs to finish at home. Although the new \$14,300 Golf has been hyped by the motor press, the cars aren't ready when VW began turning them out last September. Glitches now in production at 2,000 a day—against a target of 3,300. Still, VW officials insist the Golf is on course. "You can't measure success or failure in four to six months," says Büchelhofer.

RANKING. Perhaps not. But the study underscores flaws in the development process that could take years to fix. That's true, too, of VW's quality performance. Three surveys in Europe rank VW well behind industry leaders such as Honda, Toyota, and Mercedes. A quarter of the old-model Golfs have had mechanical problems after three years of use, vs. 17% of Toyota Corollas and 10% of C-Class Mercedes, according to a human auto inspection data.

VW trails in productivity, too. Its Wolfsburg plant still operates on a four-day, 28-hour workweek. Analysts estimate that the plant, which employs 20,000, has 20,000 to 30,000 workers too many. The Economist Intelligence Unit ranked VW's plant in Emden last in a productivity study of European car plants. Emden produced 21.3 cars per employee per year, compared with 24.5 at the top-ranked Nissan Motor plant in Sunderland, England.

Gains have come slowly. VW's workforce grew 5.4% last year—nearly as fast as unit sales. Piëch admits it takes 18 months to build the new Golf, vs. the 12 months of 20. VW officials say many recent hires are temporary workers who will be let go once the bugs are eliminated. Despite improved profits, VW's difficulties are still reflected in the bottom line. Net earnings as a proportion of sales in 1997 were 1.2%, compared with 1.8% for Ford. That should improve as VW shifts models onto four main vehicle platforms. But rivals are pursuing the same strategy, so VW has to hit a moving target if it wants to compete.

Piëch, for all his bravado, knows well that VW's situation is still delicate. He made CEO in 1993 to clean up the mess left by the overexuberant expansion plans of Carl H. Hahn. The irony is that if he isn't careful, he could find himself caught in a similar bind.

By David Woodruff in Frankfurt

COMMENTARY

By Joan Warner

GUESS WHAT? EUROPE COULD USE MORE LAWSUITS

The latest salvo in Europe's ice cream wars is enough to melt an American lawyer's litigious heart. Mars Inc., the U.S. confectioner, won a decision on Mar. 11 from the European Commission that Unilever PLC was unfairly hogging the Irish ice-cream market. Mars may now sue the Anglo-Dutch giant for damages in Ireland's national court. And it could ask for as much as \$1 billion.

Mars ought to go for it. The prospect of a billion-dollar award, paid by a powerful company to a

it's simply cheaper to go to Brussels. For \$25,000 or so, the EC's competition office will gather evidence, make a decision, and sanction or fine the offender. Lawsuits, by contrast, usually start in the six figures—prohibitive for an upstart challenging a bigfoot. In the U.S., damage awards are determined by a jury, and a company can collect triple damages for lost business. In Europe, a judge rules on the value of the missed opportunity. Plaintiffs collect only that amount.

But the anti-lawsuit culture is gradually changing.

"It's more in the consciousness of companies and their lawyers that they have private remedies before national courts,"

says Alasdair Bell, an antitrust lawyer with White & Carter in Brussels. As Germany deregulates its telecom industry, phone companies are using lawsuits to scrap for market share.

Britain's First Telecom, an upstart challenger to giant Deutsche Telekom, sued the former monopoly after DT ran a one-time ad questioning First Telecom's quality—a no-no under German law.

DT never repeated the ad, and the lawsuit generated good publicity for First Telecom. "The downside is that once you punch the big elephant," says First Telecom Managing Director Bernhard Pussel, "he gets extremely nasty." Pussel says DT's legal department now dashes off notices weekly, mainly for breaking advertising law by claiming to be cheaper.

Despite such hassles, the EC urges more cooperation between Brussels, the courts, and national regulators. The commission also has hinted that it will hike fines on companies that break competition laws. Although the EC technically can dock a violator 10% of annual global turnover, it never has done so. And it never has awarded damages to a victim. That's why a thumping private lawsuit could set a healthy precedent.

Senior News Editor Warner covers European business.



struggling rival, is just what Europe needs to push business toward free competition. Given that monopolistic practices are more the exception than the rule, a few knock-down, drag-out legal confrontations could work wonders. "More companies should be doing it," says an antitrust lawyer with a white-shoe firm in New York.

FREE FREEZERS. Complaining to Brussels is the usual course when big companies force consumers to buy goods at a certain place and price. In the ice-cream case, Unilever must stop giving free freezers to Irish retailers on condition they stock only Unilever ice cream—a decision the company is appealing. But while the EC has become more aggressive, litigation would radically raise the stakes for offenders.

By tradition, Europeans prefer arbitration to court battles, and the clubby business community eschews open hostility. With antitrust gripes,

MALAYSIA

CAN MAHATHIR GO HIS OWN WAY?

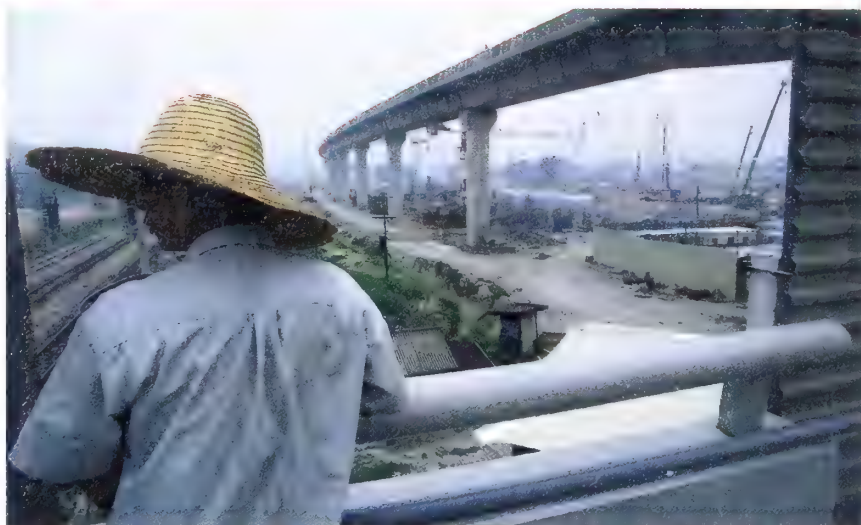
So far, he is avoiding reforms—and the economy shows it

The glittering twin towers of the Kuala Lumpur City Centre are the world's tallest buildings—and monuments to Malaysian Prime Minister Mahathir Mohamad's obsession with making his country rich and powerful. Yet the capital is buzzing with a rumor: Occupancy rates for the towers are so low that the super-rich Sultan of Brunei is buying one to bail out developers.

State oil company Petrolim Nasional, the towers' owner, denies such talk and says it has plenty of cash. Could well be. The point is that in the days of breakneck expansion, such a rumor would never have started. These are uncertain times. Mahathir swears he has a homegrown solution to pull Malaysia Inc. out of the morass of bad debts, foreign exchange losses, and slumping sales created by the crisis. But instead of inspiring confidence, the Mahathir plan is provoking murmurs of doubt. Bailing out all the banks and big companies may be a way to avoid shutting down weak institutions and shaking up industry. Some skeptics even fear that big bailouts may drive up inflation. If so, Malaysia's workout may resemble Indonesia's more than Thailand's or South Korea's. Those countries are opting for painful reforms in hopes of a quick turnaround.

DEBT DEFAULTS. This is a risky moment for the Malaysian economy. Mahathir has clearly decided to spend heavily to shore up key companies. The government has just concluded a \$500 million bailout of Sime Bank and Bank Bumiputra Malaysia, two of the nation's largest financial institutions. Rather than adopt the kinds of stringent reforms mandated by the International Monetary Fund, Mahathir and his advisers are going it alone. Because Malaysia has relatively little foreign debt, it has so far avoided an external bailout.

But internally, defaults on ringgit-de-



MALAYSE: The Kuala Lumpur rail system is one of many projects on hold

nominated debt are surging. The government is reluctant to force interest rates any higher, lest more companies default. But economists say only higher rates can check inflation and the currency's depreciation. "The pain is there," says Abdul Rashid Hussein, executive chairman of Rashid Hussein Bank, which is buying Sime Bank.

The pain is shooting through almost every corporate boardroom in Malaysia. Cellular giant Technology Resources Industries has reported a \$200 million foreign exchange loss for 1997. Politically prominent conglomerate Malaysian Resources Corp. has delayed its annual meeting as it scrambles to refinance a \$250 million bridge loan, even after it benefited from a generous purchase of its cellular unit by Telekom Malaysia.

Mahathir thinks IMF-style reforms would just make things worse. Indonesia "took the IMF medicine, and the patient died," says Rashid Hussein. By channeling local bank funds to ailing companies, he says, "we can manage it better." Adds Francis Yeoh, managing director of YTL Corp., a specialist in power and infrastructure projects: "The

IMF has too frosty a grip. We need a warmer embrace."

The Mahathir strategy typically favors a chosen few, even though the government claims such deals are legitimate transactions. Rashid Hussein Bank's \$225 million takeover of Sime Bank rescued shareholders in KUB Malaysia, which is controlled by prominent

members of the ruling United Malay National Organization. Mirzan Mahathir, the Prime Minister's son, is selling his indebted shipping empire to Petronas.

Yet a small but increasingly strident number of people in government and the business community wish Mahathir would institute reforms. The reformers apparently have the ear of Deputy Prime Minister and Finance Minister Anwar Ibrahim, who has complained to visitors about the lack of reform. "Mahathir should have let his son fail," says a UMNO activist. "That would have costed everyone and distinguished us from Indonesia. We were getting the message out that we were on track, but now what do we tell people?"

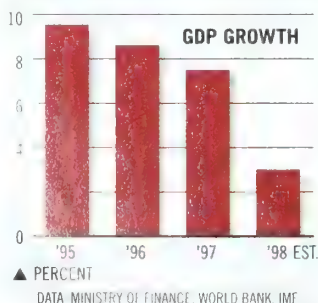
ILLEGAL IMMIGRANTS. On top of its own problems, Malaysia has to worry about the impact of Indonesia's. Thousands of illegal immigrants have come ashore in boats from the nearby Indonesian island of Sumatra. With more than 2 million immigrants already in Malaysia—most of them Indonesians—the country can ill afford more.

Malaysia's basic strengths will keep it stable. Its oil and gas production provides handsome hard-currency earnings. Prices of palm oil and rubber, two major exports, are high. Its electronics industry, though dominated by multinational companies, continues to boom.

But even with these fundamental advantages, the evidence of corporate distress increases daily. It's understandable that Mahathir wants to help his business friends. But the physician-turned-politician should remember the alternative to stiff medicine can be a patient who doesn't get better.

*By Mark L. Clifford
in Kuala Lumpur*

MALAYSIA'S SLOWDOWN



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TAKE YOUR INVESTMENTS ELSEWHERE, PLEASE

Nobel peace prize winner Aung San Suu Kyi, 52, swept Burma's elections in 1990, but the ruling military regime has never permitted her National League for Democracy (NLD) to take power. In a rare interview at the Rangoon home where she spent six years under house arrest, Suu Kyi discussed the issue of U.S. sanctions. In February, a U.S. delegation to Burma recommended some sanctions be eased on humanitarian grounds. But any investment, says Suu Kyi, strengthens the junta and undermines democracy. Companies such as Motorola, Levi Strauss, and PepsiCo have heeded this plea and pulled out. Unocal, which has an exemption for its \$1.2 billion gas project, is one of the few U.S. companies to remain.

While technically no longer detained, Suu Kyi remains closely monitored, and journalists are forbidden to meet her. On Mar. 6, Asia Editor Sheri Prasso was able to circumvent security forces and interview her.

Q: What is your reaction to the recommendation to ease some sanctions?

A: I don't understand why they want to soften the sanctions [or] on what grounds. There are those who claim the people of Burma are suffering as a consequence of sanctions, but that is not true. First of all, the U.S. did not have many investments here to begin with. As it is, there are many companies pulling out because conditions are not right in Burma for successful investment.

Q: Have there been any tangible results from the sanctions?

A: We very much appreciate the U.S. sanctions because they have been a tremendous psychological boost for the democracy movement, and also they have made businesses think carefully about what is really going on in Burma. As a result of their investigations, they have decided they really didn't want to invest here...because the economic policies



"We want investment...at the right time—when the benefits will go to the people of Burma"

AUNG SAN SUU KYI

of the government do not promote development in the long run.

Q: What message do you have for investors who want to come to Burma?

A: We want investment to be at the right time—when the benefits will go to the people of Burma, not just to a small, select elite connected to the government. We do not think investing at this time really helps the people of Burma. It provides the military regime with a psychological boost. If companies from Western democracies are prepared to invest under these circumstances, then it gives the military regime reason to think that they can continue violating human rights because even Western business companies don't mind.

Q: You met recently with Unocal Corp. President John F. Imle Jr. Did he try to persuade you to change your opposition to sanctions?

A: I never discuss my meetings...[but] we believe in talking to people, even those with whom we disagree.

Q: What is the economic climate here?

A: The economic situation is very bad. Prices are rising. A lot of businesses are pulling out. There isn't much investment coming in, if at all. The big hotels—I think they built too many to begin with—they don't have many clients and are unable to cope. The rice harvest is very poor this year. Farmers tell me it's one of the worst harvests they've ever known—in something like 60-plus years.

Q: What is the potential for civil unrest?

A: It's difficult to tell what triggers people's discontent to the point where they decide they won't take it anymore. I know there has been a lot of speculation as to whether the situation is bad enough for a general uprising. The NLD is not trying to create an uprising.

Q: There is some confusion over what to call this country. Do you have a preference?

A: Yes, Burma—because Myanmar is a name that this military regime chose when it took over. We don't think that any government, especially one that is not elected by the people, has the right to change the name of the country just because they fancy it.

Q: Under what conditions can you see a resolution to the current political impasse, such as a power-sharing agreement?

A: Everything has to start with dialogue. If anyone is interested in power-sharing, they can put it forward in the process of dialogue. We have said, with regard to dialogue, we are prepared to discuss anything.



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AND THEY’LL
SWEAT THE *details?*”

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MEXICO

MEXICO SLIPS IN AN OIL PUDDLE

As crude prices plunge, investors worry about the economy

Mexico started the year on a high note. The economy had largely shrugged off the impact of Asia's turmoil. The government of President Ernesto Zedillo Ponce de León was forecasting 5.2% growth in gross domestic product, and beleaguered Mexican workers were looking forward to their first real wage hikes in four years. Then the price of Mexico's oil fell—and fell some more, by nearly one-third, or about \$4.40 per barrel, since December.

That's scary, given Mexico's reliance on oil. Although many analysts still see bright spots, jittery investors, particularly foreigners, are shunning Mexico's stock market. It's down 14.1% in dollar terms this year (chart). American depositary receipts of blue chips such as steelmaker Hylsamex and construction giant Grupo ICA are off 28.2% and 27%, respectively. "A few months ago, it was the Asian crisis—now it's the oil crisis," says Raymundo Winkler, director of the Center for Private Sector Economic Studies in Mexico City. "Until the dust settles, investors will be nervous."

What's making them wary, after last year's exhilarating 52% rise in the *bolsa*, is the damper on the economy from oil's collapse. Lower oil prices mean less revenue for the government and a widening trade gap that puts pressure on the

peso. Although oil accounts for only 10% of Mexico's exports, state oil monopoly Petróleos Mexicanos provides almost 40% of government revenues—which shrink by \$800 million for each dollar that oil prices drop. In response, Zedillo's team cut spending by \$1.8 billion in January and recently tightened monetary policy to fight inflation.

While that's prudent, analysts expect the moves to trim GDP growth to 4.7% or less. What worries portfolio investors is the potential brake on corporate profits and stock prices. With more spending cuts likely, people are "waiting for the other shoe to drop," says Gray Newman, Latin America economist for HSBC Securities Inc. Some investors have left for Brazil, where São Paulo's market has risen 14% this year after recent free-market reforms and privatization plans.

Mexico's trade balance, as well as its budget, is being hurt by the price drop at a time when imports have been spurred by last year's 7% GDP growth. The result is downward pressure on the peso, off by 6.4% so far this year, and

upward pressure on consumer prices. They rose almost 4% through February, putting the government's 12% inflation target for the year out of reach.

While the uncertainty has made investors sit tight, their skepticism puzzles many Wall Street analysts who are relatively upbeat about Mexico. That's because of the continuing momentum from last year's consumer recovery. In the crisis after the 1994 peso devaluation, Mexican workers lost a quarter of their purchasing power. But now

employers are starting to give pay raises of 19% or so. That will give a further boost to long-depressed consumption.

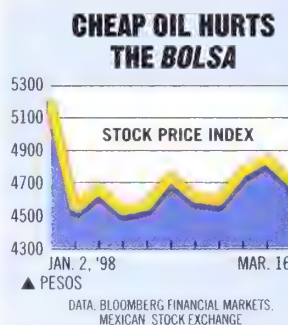
BOND BETS. There are other positive signs. At a breakfast this month in Los Pinos, Zedillo's official residence, executives of 199 multinationals such as Ford Motor, Sony, and Philips Electronics pledged to invest \$10.5 billion in Mexico this year, creating 46,000 jobs. The inflow will cover a good chunk of Mexico's current account deficit, which could hit \$14 billion this year as imports rise. And in the global bond market, Mexico placed a \$415 million, 15-year Italian lira issue on Mar. 17, just two weeks after a \$1 billion, 10-year global bond issue in the U.S. "The debt market

seems to be shrugging off concerns," says Eduardo M. Cabrera, chief Latin America strategist for Merrill Lynch & Co. in New York.

Most analysts believe it's time for a turn around. They are mostly bullish on stocks that will gain from rising consumer demand, such as brewer FEMSA and retailer Soriana, even

though FEMSA's ADRs are down 12.9% and Soriana is off by 13.1% on the *bolsa*. They also like bellwether Teléfonos de México, though its ADRs are off by 2.9% for the year. But discordant voices, such as Salomon Smith Barney's Latin equity strategist James W. Barrineau, warn that earnings may look flat this year after 1997's strong growth. And as oil prices slide, such voices are the ones that investors seem to be heeding.

By Elisabeth Malkin in Mexico City



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— Olli Kallasvuo,
President,
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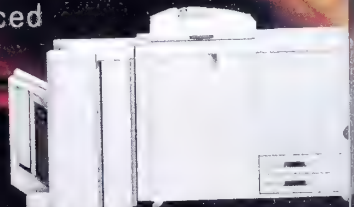
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EDITED BY JOHN TEMPLEMAN

WHY THE STRAITS OF TAIWAN ARE LOOKING CALMER

After nearly three years of standoffs and saber-rattling, Taipei and Beijing are close to resuming talks that China broke off after Taiwan President Lee Teng-hui's 1995 visit to the U.S. Beijing took the first step by offering a major concession. Instead of insisting, as before, that the reunification of Taiwan with China be on the agenda, Beijing is now ready to discuss practical matters such as fishing rights without raising the charged reunification issue. One Chinese official says Beijing also may offer to announce the use of force in its dealings with Taiwan to smooth long-term discussions about reunification.

Powerful forces are shaping China's new policies. President Jiang Zemin is due to hold his first summit with President Clinton this summer. China's ambitious economic makeover, masterminded by Premier Zhu Rongji, could draw more Taiwanese knowhow and investments. At the same time, Beijing is nervous about the rise of Taiwan's opposition Democratic Progressive Party (DPP) and the possibility that it might fan support for independence. Analysts think the DPP will advance in general elections next year, and a tough Chinese stance on reunification would only advance the DPP cause. President Lee can't afford to get sucked into talks about reunification, either. Taiwan's newly enfranchised voters are deeply divided on independence. Most favor the present ambiguous situation, but polls show the proportion favoring independence is growing. "Lee's interest is to keep the status quo as long as possible. There's no consensus in domestic politics on the China issue," says Andrew Yang, secretary general of the Chinese Council for Advanced Policy Studies. Few talks could sharpen differences. The issue of who Taiwan won't stay in the background forever now that Hong Kong is back in Chinese hands. Beijing insists it wants

to move "step by step" and not force reunification talks—but they're still the objective. And Taiwan worries that Beijing will exploit the discussions to divide domestic opinion by, say, encouraging executives to press for direct flights to China.

PRESSURE. Despite Beijing's new line, old animosities lie close to the surface. China's Foreign Minister angrily denounced Taiwan on Mar. 12 for dragging its feet after Beijing offered to resume talks. He accused Taiwan of creating trouble in Southeast Asia—first in October by devaluing its currency and now by offering investment cash to win allies. "[They] want political rewards," says a Chinese official.

Indeed, Taiwan is busily seeking new friends because it feels pressured by the U.S. to negotiate with China. A string of former U.S. officials and academics—such as former Defense Secretary William Perry and Joseph Nye, dean of Harvard University's Kennedy School—have visited Taipei this year to urge talks with Beijing. "The U.S. is doing everything except overtly pressure Taiwan, but the pressure is real," says National Taiwan University political science Professor Chu Yun-han.

It could hardly be otherwise. At his summit with President Clinton last year, President Jiang won a renewed U.S. commitment to the one-China policy. Taiwan's courtship of Southeast Asia is hardly a counterbalance. Taiwan got a foot in the door with countries that don't officially recognize it, such as Malaysia. But these new friends aren't likely to stick their necks out and anger China.

The hard reality doesn't change. Beijing may use a more patient and less confrontational policy, thus easing regional tensions. But China's leaders are unswerving in their ultimate goal—they want to reclaim control of Taiwan.

By Jonathan Moore in Taipei, with Joyce Barnathan in Beijing



ANGRY: Independence rally

GLOBAL WRAPUP

WINDY PRAISE FOR JOSPIN

The first round of French regional elections on Mar. 15 gave a weak endorsement to Socialist Prime Minister Lionel Jospin. His left-wing coalition set to win at least 10 of France's 22 regions, up from 2 in 1992. But abstentions ran at 42%, high for France. And extreme parties on the left and right made gains, with Jean-Marie Le Pen's extreme-right National Front garnering nearly 16% of votes. The rising tides of extremism and apathy make it hard for Jospin to

move the left toward the center and prepare France for global competition. Moderate-right parties, meanwhile, are still in disarray. Unwilling to align with Le Pen or rally behind a centrist platform, they seem destined to remain in opposition for some time.

POWER GRAB IN SLOVAKIA?

► Slovak opposition groups plan a big demonstration against Prime Minister Vladimir Meciar on Mar. 25. They say Meciar wants to set up a one-party dictatorship. He assumed interim presidential powers on Mar. 4, after

President Michal Kovac's term ended. Meciar lost no time in throwing his weight around—replacing all but one of Slovakia's ambassadors.

Opponents say Meciar intends to make himself President with enhanced powers—and change electoral laws to stifle opposition. Legally, he can act as President until the Slovak Parliament, which he controls, elects Kovac's successor by a two-thirds majority. Meciar's ambition could cost Slovakia plenty. Already, his disregard for human rights has kept the country off the fast track to join NATO and the European Union.

CONSERVATION

ONLY GOD AND TOYOTA CAN MAKE A TREE

The carmaker is cultivating a smog-eating forest

In the labs of Toyota Motor Corp. outside Nagoya, 40 researchers are working to improve an unlikely object: the tree. To counteract environmental damage from car and truck exhaust, Toyota is developing unique trees that can absorb some of the toxic gases contained in smog and might help prevent global warming.

There. Trees absorb a lot of carbon dioxide, and genetically engineered trees might do even better.

Toyota is not alone. Royal Dutch/Shell will spend \$500 million over the next five years planting forests in Chile and New Zealand to absorb carbon dioxide. Shell is also trying to find cleaner ways to burn wood, rather than oil, for fuel. In Japan,

the versions with double chromosomes

He has since refined his technique so that it works in as many as six seeds out of 100. Toyota applied for a patent in 1995 and sought a second patent in 1997 when Matsui discovered that his super-trees withstand salty ocean winds. Today, Matsui nurses 50 different varieties of the trees on a plot near Toyota's factory. In lab tests, his designer eucalyptus trees absorb up to 30% more nitrous oxide than the average tree, while altered London plane trees absorb 20% more. Matsui still must determine whether the trees perform as well outdoors, and whether they do any damage, such as taking up more than their share of soil nutrients.

Indeed, some environmentalists say Toyota is headed in the wrong direction. "If we want to reduce [nitrous oxide]



WHY TOYOTA'S TREES ARE SO SPECIAL

- ▶ The pores on their leaves that absorb greenhouse gases have been enlarged and strengthened
- ▶ They absorb as much as 30% more smog in labs than regular trees
- ▶ They also withstand salty ocean winds longer

MATSUI: Putting twice as many chromosomes in the tree

Why is Japan's No. 1 carmaker dabbling in the agricultural arts? It's all part of an effort to establish itself as the

world's greenest carmaker. Last December, Toyota became the first auto maker to bring to market an affordable hybrid car—powered by electricity and gasoline. In 1991, Toyota researchers began work on biology-based ways to clean up the environment. They launched Forest of Toyota, a project ranging from planting more trees to developing smog-eating plants.

COOL SHADES. The effect of Toyota's re-engineered trees won't be huge—it takes 20 regular trees to absorb the noxious gases of just one car in a year. But Toyota says it can improve that performance by 30%—and that's better than doing nothing. Toyota is also probing the potential of trees to prevent climate change. Global warming can be caused by a buildup of carbon dioxide in the atmos-

phere. Trees absorb a lot of carbon dioxide, and genetically engineered trees might do even better. Toyota is not alone. Royal Dutch/Shell will spend \$500 million over the next five years planting forests in Chile and New Zealand to absorb carbon dioxide. Shell is also trying to find cleaner ways to burn wood, rather than oil, for fuel. In Japan,

the Forestry Agency is examining how timberlands, which cover 70% of the country, can absorb more of the estimated 320 million tons of carbon dioxide that Japan generates every year. "Now, more people are researching what use our forests have, not in terms of wood products but in terms of our ecosystem," says Kazuo Suzuki, a botany professor at Tokyo University.

Kunio Matsui, the chief botanist on Toyota's tree project, says the goal was to create trees that absorb toxic gases such as nitrous oxide and sulfur dioxide found in smog. These can kill trees. But Matsui found that doubling the number of chromosomes in experimental trees widened the tiny air inlets on stems and leaves. Afterward, the inlets absorbed more nitrous oxide than in standard trees.

Matsui's methods weren't particularly efficient. He treated seeds of gum trees, conifers, broad-leaf trees, and London plane trees, but could make only two out of 10,000 seeds metamorphose into

we should reduce our automobile production and set lower emission standards," says Yuichi Sato, deputy director of research at Japan's Forestry Agency. Another part of the Forest of Toyota project is an \$800,000 model forest the company created last year next to a resort called Foresta Hills. The forest will soon be monitored with \$80,000 worth of emissions-measuring equipment so Toyota can test the impact that different forestry techniques have on reducing carbon dioxide levels. Company researchers are also trying to grow trees in acid-drenched soil, a technique that could be used to restock ravaged rain forests in Southeast Asia.

Meanwhile, Toyota wants to line the highways of Japan with old-fashioned trees to absorb more carbon dioxide but must first win permission in overregulated Japan. Building a better tree is only half the battle—Toyota must still fight to plant them.

By Emily Thornton in Tokyo

RE DRUG ADS A URE-ALL?

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backfired with consumers. And since
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LEEWAY. Even so, that uncertainty
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s are surging, thanks to record num-
of new products. That has intensified
et share battles, leaving drugmakers
pe alluring ads will help them win
mer loyalty. "The days of products
ng a five-year window without com-
on are gone," says Stephen S. Tang,
al director of A. T. Kearney Inc.'s



pharmaceutical consulting practice. "Any significant therapeutic class now sees competition within six to nine months."

That's why drugmakers cheered changes in their advertising rules. Before the FDA guidelines were revamped last August, consumer drug ads on TV and radio either named the ailment or the drug—but not both, a restriction that kept many companies from even trying. Now, the ads can include both information on the product and the illness as long as they give leads for more information and a summary of the major risks. That new leeway sent radio and TV drug ad spending soaring last year, more than doubling in 1997, to \$167 million, according to Competitive Media Reporting, a firm that tracks ad spending. Total drug ad spend-

ing, including print, TV, and radio, is expected to top \$1 billion in 1998.

Freedom, however, comes with its own set of problems. In the category of allergy relief, drugmakers hope that advertising will help them catch Schering-Plough Corp.'s Claritin, which boosted its U.S. sales 350% over three years, thanks in part to an aggressive campaign of consumer ads. Glaxo Wellcome PLC spent \$42 million on its ad blitz last year for allergy-relief nasal spray Flonase.

While Glaxo says that it was pleased with the campaign's impact, the result was a less-than-stunning \$47 million U.S. sales gain.

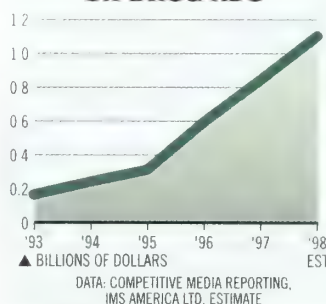
Hoechst Marion Roussel Inc., too, is in the allergy marketing act, spending a hefty \$64 million on its consumer campaign last year for Allegra. Pfizer Inc. was not far behind, with a \$51 million media blitz for its own allergy product, Zyrtec. Sales for both are strong. But pharmaceutical officials say they're unsure how much of the growth is thanks to consumer advertising, vs. the more traditional promotion efforts, such as ones aimed at doctors. "Because of all the advertising [of allergy

drugs] now, it is much harder to measure," says Diane Parks, head of marketing for Allegra.

WILD CARD. Adding to their difficulties, drugmakers still must contend with a powerful third party in their consumer marketing: doctors. A strong medical consensus can easily eclipse millions of dollars spent on brand-building. Consider the ad spending by Merck & Co. and Bristol-Myers Squibb Co. on their

cholesterol-lowering drugs. Bristol's push for Pravachol was the most expensive ad campaign of last year, according to Competitive Media Reporting, nearing \$67 million. Merck spent close to \$46 million promoting its cholesterol drug, Zocor. Both saw strong sales growth of 36% in 1997, with Zocor and Pravachol sales hitting \$1.4 bil-

HEALTHY SPENDING ON DRUG ADS



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on page 198

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Marketing

lion and \$768 million, respectively.

But both are quickly being challenged by another drug, Lipitor, which did no consumer advertising. Lipitor, launched in February, 1997, by Warner-Lambert Co., was promoted to doctors through a marketing partnership with Pfizer. Because of the drug's exceptional ability to lower LDL cholesterol—the so-called “bad” cholesterol—physicians made Lipitor the fastest-growing drug in the category. Sales last year jumped to \$583 million, and Lipitor is rapidly gaining on its high-spending rivals. Says PreTesting's Weinblatt: “If the physician is aware of what they think is a better alternative, consumer advertising will be very ineffective.”

FALLING ON DEAR EARS? Part of the problem for the drug companies is that perhaps as much as half the population isn't particularly receptive to their ap-



ALLEGRA: A later entry in the allergy wars, it must cut through ad clutter

was revealed that their pharmacies were sending names and addresses of patients to an outside direct-marketing firm. That company then sent out letters to patients who had prescriptions for products such as Merck's Zocor to help

remind them to take their medication—and also, of course, drive the sale of refills to their brands. Consumers worried that their pharmacies were letting intimate medical information loose into the hands of marketers. While the retailers maintain no confidentiality was breached, they were stung by the response. Both companies dropped the program.

Despite a sometimes painful education, pharmaceutical companies are unlikely to back off their consumer advertising of



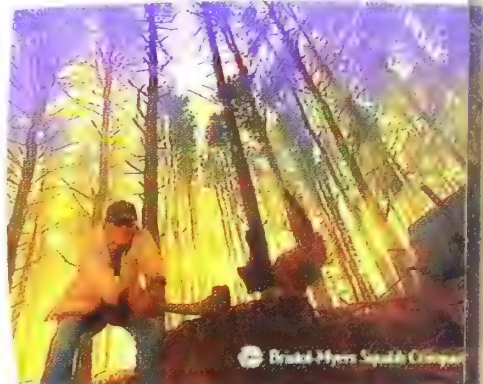
CLARITIN: A massive spending pushed sales up 350% in three years

peals. As it turns out, men are far less likely to suggest a brand-name drug to their doctors than women. A study by Health Medical Consumer Advertising & Marketing found 29% of women asked their doctor about a branded prescription drug, vs. just 14% of men. Pfizer learned that the hard way, spending \$14 million on a print campaign for Cardura, a drug for benign enlarged prostate—with limited success. “In diseases that are primarily male, there may be more effective ways to communicate than talking directly to the patient,” says J. Patrick Kelly, a vice-president at Pfizer.

Sometimes, communication can even lead to consumer backlash. In February, both CVS Corp. and Giant Food Inc. came under fire when it

fensive. And, for now, the risk of physician backlash, once a huge potential obstacle, seems less likely. “I don't like it,” says Dr. Donald Miller, a rheumatologist in Bryn Mawr, Pa. “But it hasn't created a major headache for me.” Until they master the world of consumer branding, drugmakers may find that they are the ones suffering the real headaches.

By Amy Barrett in Philadelphia



PRAVACHOL: Spent big, but one major rival ran no consumer ads

Culley

ries about construction
ays (50% chance of rain),
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ect instability in Asia
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BASEBALL

PITCHING 100 MPH IN PHOENIX

Can Jerry Colangelo make the Diamondbacks sparkle?



Ah, spring training in Arizona. It's a time when baseball fans settle into cozy stadiums close enough to the field to banter with their favorite heroes or grab an autograph. But on this day in Hohokam Stadium, just east of Phoenix in Mesa, the fans stream past slugger Matt Williams for the star of the moment. Decked out in black silk pants and a white polo shirt, Jerry Colangelo sits in a first-row seat behind the plate. One by one, the fans shove programs, baseballs, even a water bottle at the man who brought Major League Baseball to the desert. Says Colangelo: "The moment they stop asking, it means you're in trouble."

Colangelo sure isn't in trouble just now. The 58-year-old onetime college basketball star is spending big-league dollars to give a sports-crazed state a baseball team. By all accounts, his Arizona Diamondbacks probably will finish dead last in the National League's five-team Western Div. But so what? With season-ticket buyers holding nearly three-quarters of the 48,569 seats in a \$350 million new stadium in Phoenix—even before the team takes the field on

JERRY COLANGELO

BORN Nov. 20, 1939

CAREER

1966 Head scout and director of merchandising, Chicago Bulls

1987 Led group that bought Phoenix Suns for \$44.5 million

1995 Landed Major League Baseball expansion franchise in Arizona

OWNERSHIP

36%* of Phoenix Suns pro basketball team, worth \$200 million

1%** of Arizona Diamondbacks baseball team, worth \$350 million

36%* of license for Phoenix Mercury of WBNA, worth \$25 million

25% of Arizona Rattlers arena football team, worth \$50 million

* Controls management group that owns 36% of teams

** Colangelo management group has options to purchase up to 25% of team

DATA: TEAM INFORMATION, BUSINESS WEEK ESTIMATES

Mar. 31—the Diamondbacks are all but assured of placing among the leaders in attendance and operating profits.

That would only add to Colangelo's winning streak, which started not long after he came to Phoenix in 1968 with wife, three young kids, and "a couple hundred bucks in my pocket." To the Phoenix Suns basketball team that he controls and owns 36% of has sold 369 straight games—second only to the Chicago Bulls' 519. He has made money as well with the year-old Phoenix Mercury, which led the Women's National Basketball Assn. in attendance, and the Arizona Rattlers, last year's Arena Football League champs.

But nowhere are the stakes higher than with the Diamondbacks, which have cost Colangelo and his cadre of mostly corporate investors

SPLASHY

Colangelo's fancy new stadium includes a swimming pool that overlooks right field

more than \$325 million to put on the field. That sum includes a record \$130 million expansion fee the Diamondbacks paid and \$100 million that they paid toward construction of

\$350 million state-of-the-art stadium. And that's not counting the \$100 million plus that the Diamondbacks spent on field a team. Colangelo committed a total of \$79 million to two players alone: Williams and shortstop Jay Bell.

MARLINS REDUX? Baseball historians don't have to go back far to find teams that spent their way into woe. Ten years back, the Florida Marlins paid \$89 million to free agents. They won the World Series last year, but owner Larry Wayne Huizenga was forced to put the money-losing team up for sale and did off its stars. Colangelo "still hasn't proven that people are going to watch baseball in those hot desert summers," says Colorado Rockies owner Jerry McMorris, whose franchise, the most profitable in baseball, is Colangelo's model.

Sitting behind the screen watching his team on its way toward beating the Chicago Cubs 9-8, Colangelo fairly bites at charges by New York Yankees owner George Steinbrenner and others that he is overspending. His player payroll, he says, is a little more than \$70 million for the year. "And I'm getting criticized by folks that have \$70 million



UNLIMITED PARTNERSHIP

MIKE ROBERGE FROM ARAMARK with RALPH SCURFIELD FROM SUNSHINE VILLAGE IN BANFF, ALBERTA, CANADA

REVENUES ARE UP

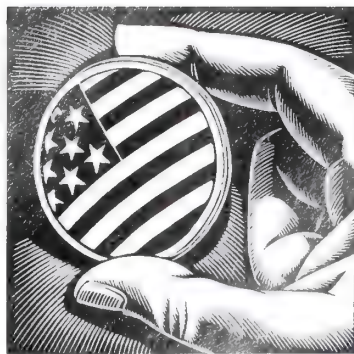
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Our partnership with ARAMARK began when we did a major expansion of ski terrain," says Ralph Scurfield of Sunshine Village. "The challenge to Mike Roberge and ARAMARK was to help us make our food service every bit as good as the skiing. And they did. In the first year they revised menus and redesigned our existing facilities. The following year they added 600 new dining seats at eight locations and even turned an unprofitable "brown bag" area into a busy "ski-to" lounge. This year, we've expanded our partnership to include an apprenticeship program with special training and opportunities for young people." At ARAMARK we know "raising the bar" calls for proactive thinking. So we don't just tell partners what to do, we do it for them – from consultation through operation. And that approach always finds its way to the bottom line. Adds Ralph, "Revenues have increased by 50% and per cap spending is up 17%. And better still the *Rocky Mountain Express News* rated our food best on-mountain and *Snow Country* voted us the #2 ski resort in Canada."

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Sports Business

payrolls," he says. He predicts the team will draw 3.5 million fans this year, up there with leaders like the Rockies and the Los Angeles Dodgers. And what about largesse such as the \$45 million he's paying 32-year-old Williams over five years? "These are hardly irresponsible deals," he says. "We are signing players that will be role models for the team and solid citizens for their community, as well as play the game well."

Just as Williams can hit a fastball, Colangelo knows how to market to fans and partners alike. "When Jerry looked for investors in his sports team, we all wanted in," says John Teets, former chairman of Dial Corp., which bought into the Suns and the Diamondbacks. The team ownership group Colangelo has this time includes the state's two major dailies, its three largest banks, its biggest mining company, and America West Airlines Inc. Many of them also kicked in to help the team raise an impressive \$500 million in marketing revenue, including \$140 million that team investor Bank One paid to slap its name on the stadium.

The formula of high-priced talent and corporate sponsorship has driven the Suns since 1987, when Colangelo put together a corporate group to buy the then struggling team for \$44.5 million. Many Diamondbacks employees, including President Richard H. Dozer, come from the Suns. The two teams also share an ad agency, SRO, which just happens to be controlled by Colangelo's management group. Few teams, however, can match the Diamondbacks' new stadium. Sitting under a retractable dome, it boasts 69 luxury boxes, six party suites, and a microbrewery and restaurant. And let's not forget the swimming pool overlooking right field, which already has brought in \$600,000 in ads from a pool chemical company.

HUSTLING. Such business acumen has made Colangelo a five-time winner of the *Arizona Business Gazette's* Executive of the Year award. That's a long way from the gritty Hungry Heights neighborhood of Chicago Heights, where Colangelo grew up with dreams of being a big-league baseball player. A sore arm turned him to basketball, and he became an All Big Ten selection at the University of Illinois. Although he played semi-pro after college, it was selling that really fired him up. "He was a hustler all his life," says Frank Nar-

cisi, a friend from Chicago who ran a tuxedo-rental business with Colangelo in the late '50s and early '60s.

Colangelo's training to run a professional sports operation came when he worked with Dick Klein, a Chicago consumer marketer. When Klein proposed applying for what became the National Basketball Assn. franchise to own the Chicago Bulls, Colangelo lined up investors to raise the \$1.25 million franchise fee. In 1966, when the Bulls took the court, Colangelo was its head scout and merchandising director. Two years later, at 28, he went to Phoenix to put together the Phoenix franchise.



THROWING MONEY

The Diamondbacks paid \$45 million over five years for 32-year-old slugger Matt Williams, and fans are snapping up season tickets

Colangelo and the laid-back Arizona lifestyle are among the reasons that All Stars such as Danny Manning ignore better offers and joined the Suns. But not everyone is enamored of Colangelo. Two years after he helped them relocate from Winnipeg, the Phoenix Coyote hockey team is losing money—in part, claims owner Richard T. Burke, because Colangelo misled him about the revenue the team could generate from the Colangelo-run arena. "It's our own fault, I guess," Burke recently told the *Arizona Republic*. "We chose to believe people meant what they said."

Colangelo argues that the Coyotes have a better lease than the Suns—and notes that the Coyotes still have three years on a five-year lease, so things could change. Then he turns back to his latest project, the Diamondbacks, who are rallying for four runs against the Cubs. A week of celebrations, including a black-tie symphony concert, is planned for the opening of the stadium. The megaprofitable Rockies come to town for the first official game on May 31. That's one team Jerry Colangelo intends to beat—both on and off the field.

By Ronald Grover in Mesa, Ariz.

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INTERNET

MR. BOHNETT'S CYBERHOOD

First, GeoCities offered home pages. Now it's bringing in online shops—and preparing to go public



It's a beautiful day in the neighborhood. Just ask "Grandma." She lives 11 miles from her nearest neighbor—and three miles from her mailbox—on Little Stony Mountain in West Virginia. But these days, she's spending lots of time in Heartland, her GeoCities cyberhood. Her address: www.geocities.com/Heartland/Plains/6501. "I'm a Geo junkie," says Grandma, a disabled grandmother who prefers anonymity. "It's my main contact with people."

With more than 1.5 million cybernauts homesteading in 40 different GeoCities neighborhoods, such testimonials are endless. That's exactly what David Bohnett, a 42-year-old former marketing executive at software company Legent Corp., was banking on when he set out in 1994 to create a giant Internet community. Bohnett (pronounced BO-net) bet that if he gave away Web space and home-page publishing tools and created neighborhoods built around common interests or hobbies, Netizens would pour in. Sure enough, TV and movie buffs flocked to create addresses in the Hollywood neighborhood, nerds migrated to Silicon Valley, and small investors converged on Wall Street.

It's a land-office business. GeoCities is signing up new members at a rate of six per minute. In February, Geocities.com was the seventh most visited Web site, according to Web-traffic monitor RelevantKnowledge. It was the second-

fastest-growing Web site last year, after Bluemountainarts.com, an electronic greeting-card publisher. The result: GeoCities racked up \$6 million in revenues last year, 80% from advertisers keen to target specific neighborhoods.

Now, Bohnett thinks he can quadruple revenues, to about \$25 million this year, partly by adding online stores to the neighborhoods. This month, a new program called GeoShops will let Netizens open electronic storefronts for \$24.95 a month. For an extra \$40, plus 5% of sales, they can plug into GeoCities' order- and transaction-processing system, including credit-card verification and

FOUNDING FATHER: Chairman Bohnett is on the lookout for a CEO

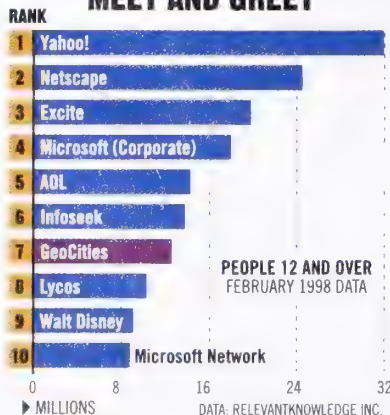
sales-tax calculation. Bohnett figures more than 100,000 entrepreneurs will hang their shingles during the first year.

This is no ordinary electronic marketplace—an approach that has flopped on the Net. Instead, online merchants can pick neighborhoods where people of like minds hang out and chat. A maker of hand-tied flies for trout seekers, for example, could opt for Yosemite, an area for outdoor sports fans. "It's like AOL ladies online, where ordinary people become a sales force," says analyst Kay Delhagen of Forrester Research Inc.

Corner cyberstores is just GeoCities' latest foray into E-commerce. In recent months, the Santa Monica (Calif.) startup signed deals with online retailers such as bookseller Amazon.com, record shop CDnow Inc., and credit card company First USA Visa. They get a prominent and exclusive placement on its site—and GeoCities gets a cut of the revenues, an arrangement that could bring millions to GeoCities.

The startup has already proven it can draw the advertising dollars—some \$4.8 million last year. By letting companies zero in on specific neighborhoods, GeoCities appeals to 40 to 50 advertisers at any given time, including Ford, Microsoft, M&M's, and Cathay Pacific. "What intrigued us about GeoCities was

WHERE CYBERNAUTS MEET AND GREET



ability to target the auto enthusiasts neighborhoods," says Jon Bucci, inter-communications manager for Toy-motor Sales USA Inc., a Motor City tiser.

it's fees from shopkeepers and ue-sharing from the giant online ers that will propel GeoCities into ic offering and profitability this Bohnett says. In 1998, he figures ties will report between \$20 mil- and \$25 million in revenues, 70% t from advertising, including the tional fees and commissions paid exclusive commerce partners. The ill be monthly rent and commis- from GeoShops.

preparing for its IPO, GeoCities is g a professional management team. d an ad chief from Disney Online, el G. Barrett, and a CFO, Stephen nsen, from Universal Studios. Next a CEO to replace Bohnett, who will n as chairman. Says Bohnett: "My ound is software, but what we re- eed is a savvy media or publishing ive." He expects to name a new n a few months.

ORS. Success means competition, eoCities already has a batch of im- , including such sites as The Globe, fire, and FortuneCity. In Febru- s biggest rival for free Web space, Inc., was snapped up by search- company Lycos Inc. for \$58 million ck. Success also has meant buyout —GeoCities says it had two last t won't name the companies. In- in January the company raised illion from Softbank Holdings Inc. 5 million from search engine Ya- nc.—for a combined stake of 32%. GeoCities can stave off the compe- and keep growing, will it lose its own appeal? Already some are g. Last fall, the company decided ers had to accept ad banners or o advertising on their sites. That some homesteaders away.

most GeoCities' residents are with their free Web homes—even Schalehlin, who's decamping soon s own site. Two years ago the -songwriter in North Hollywood, set up a page in the Broadway oorhood to keep a diary so his ers in Texas could follow his fight t AIDS. The resulting publicity led Off-Broadway production of a me- ne'd written, *The Last Session*. Schalehlin wants his own domain "But I'll always keep the GeoCi- nk," he says. It's that kind of loy- hat Bohnett will need to grow ties into a major metropolis.

Larry Armstrong in Santa Monica

ANOTHER NET IPO FRENZY —WITH A DIFFERENCE

Spring is warming up fast for Internet IPOs. On the heels of successful offerings by VeriSign, DoubleClick, and cDnow, whose share prices have risen between 50% and 220% above their asking prices, bankers are scrambling to find candidates they can throw at investors hungry for Net stocks. "We're in the strongest market for Internet IPOs since we took Yahoo! public two years ago," says

high-tech IPOs, according to Securities Data Co.

Still, this isn't shaping up to be a repeat of the 1995 Net IPO frenzy, when any company with a promise went public. Startups now boast higher revenue, more Web traffic, and seasoned management teams. ISS Group Inc., for example, is an Atlanta provider of network-security monitoring software. With 1997 revenues of \$13.5 million and a \$3.9 mil-

The Sizzle Is Back

COMPANY	IPO STOCK PRICE	CURRENT STOCK PRICE
VERISIGN Makes security software and digital certificates for the Internet	Jan. 29 at 14	44 ¹¹ / ₃₂
CDNOW One of the pioneers of selling CD-ROMs on the Web	Feb 10 at 16	23 ¹¹ / ₁₆
DOUBLECLICK Places ads for advertisers across a network of Web sites	Feb. 20 at 17	35
PC CONNECTION Sells PCs, hardware, and software via the Web, catalogs, and telemarketing	Mar. 2 at 17 ¹ / ₂	19%

DATA: BUSINESS WEEK, BLOOMBERG FINANCIAL MARKETS

Bradford C. Koenig, a managing director at Goldman, Sachs & Co.

That's a turnabout. Many Internet companies sat on the sidelines last year as stocks stumbled after the initial Web euphoria. No more than two companies a month have gone public since July, 1996, with Net IPOs dropping to 12 in 1997 from 21 the year before.

Now there's a new attitude. As anxieties over the Asian crisis ease and Net companies show staying power—highfliers Yahoo! Inc. and Lycos Inc. are turning a profit—investors have warmed to the group. The big thaw, though, comes from reports of lower than expected earnings from Intel Corp. and Compaq Computer Corp. The computer industry giants are suffering lower margins brought on by the explosion in sub-\$1,000 PCs—a trend that's sure to bring more people to the Web. The news sent the stocks of search engine Yahoo! and Internet book-seller Amazon.com Inc. to all-time highs the week of Mar. 9. This month, there already have been nine

lion loss, it's slated to go public on Mar. 23 at 14 to 16 a share. Compare that with the \$127,400 in annual sales CyberCash Inc. had when it went public in 1996.

READY TO GO. Others are lining up to go. Verio Inc., an Englewood (Colo.) Internet service provider with 1997 revenues of \$77.9 million, has filed, and so has Exodus Communications Inc., a Santa Clara (Calif.) provider of network management services with sales of \$7.5 million through September, 1997. Other likely candidates, say analysts and bankers, are Vignette and NetObjects, which help companies publish Web sites. And GeoCities, the seventh-most-visited Web site, which lets Netizens post their home pages for free, is expected later this year. "The IPO track is certainly what we have in mind," says Peter Mills, a managing partner at CMG @Ventures LP, a GeoCities investor.

They had better hurry. Between investor whims and El Niño, who knows what summer holds.

By Heather Green in New York

YEAR 2000

EXTERMINATING THE MILLENNIUM BUG

On the scene with a medical insurer's SWAT team



➔ Mary Libens briefs Medical Mutual of Ohio's help-desk team on the kinds of problems they can expect in 2000

➔ The Y2K team needs to be able to reach Libens at all times. The brainstorming continues at home and on the road



The good news: Mutual's critical systems should be shipshape by the end of 1998, allowing for a full year of testing. When the final bell tolls, Libens is confident that no major system will bump into a date that reads "00," interpret it as 1900, and run amok. But it has been a slog, even when tons of time and resources. And though all may end well, Mutual's travails and harrowing discoveries make it a chilling case study for any large company that is just heading down the Y2K obstacle course.

The majority of big corporations like Mutual have spent much of the past 40 years adding new computers and

software willy-nilly to their data centers, building up great Augean stables of information and a tangle of jerry-built routines. With Y2K, for the first time they will be forced to sift through these diverse systems. The programs they devise to remedy the date bug—like any software—will be imperfect, causing new glitches. And at this late date, companies could have trouble listing the aid of qualified consultants, most of whom are already tapped at assisting customers that signed up early. As the clock ticks, programs slapped together will produce increasingly



➔ Team members meet every Tuesday at 9 A.M. to go over the week's schedule. But informal meetings continue throughout the week

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satisfactory results. The problems, says Libens, "are overwhelmingly huge."

Mutual owes its early start to Libens' boss, Chief Information Officer Kenneth Sidon. Early in the decade, Sidon recalls that the millennium bomb "was something we kidded about." But when he began to consider the implications for Mutual, then known as Blue Cross/Blue Shield of Ohio, all joking stopped. In 1995, he began combing through the company's systems and was aghast at what he discovered: a dizzying total of 25,000 computer programs, many added through three acquisitions made over the previous decade. All told, Sidon counted 70 distinct operating systems at work in 36 locations across several states.

The hardware diversity was equally horrific—a hodgepodge supplied by 64 different vendors. In one basement office, an ancient IBM mainframe toiled away. In another stood a spanking-new Hitachi mainframe, running a different operating system. PCs—some 3,300—were linked in heterogeneous networks managed by UNIX and Windows NT servers. These shared work with about 800 1970s-era "dumb terminals."

Incredibly, the hodgepodge performed just fine for years, processing a million claims for Mutual each month with nary a hitch. But Sidon knew this would unravel when it ran up against the millennium. Surveying the awesome complexity, he made a key decision: Mutual would fix as few dates as possible so it could focus all its resources on the dates that mattered.

DIGITAL TRIAGE. Some of the calls were no-brainers: Birthdates would all get remediated because any system handling a claim in the year 2000 would need to know whether a customer born in "99" was a baby or a 101-year-old. For the rest, Sidon's team began sorting programs into three categories. Marked for oblivion were all customized programs that would be obsolete by the Year 2000. A second group, deemed low-priority, included those programs whose dates weren't critical to operations. The third group consisted of software from outside vendors such as Electronic Data Systems, IBM, and hundreds of smaller players, which Sidon felt should be fixed by the supplier.

At this juncture, Sidon was handed another nasty surprise. Some suppliers had never gone back and tested their products for Y2K compliance. Many of the smaller companies were no longer in business. Some who were still around tried to turn Mutual's emergency into a sales opportunity, asking Sidon to buy

COUNTDOWN TO THE YEAR 2000



1995 CIO Ken Sidon, looking into the Year 2000 glitch for the first time, orders an inventory of all the company's computers and software. He finds 25,000 programs, two-thirds of them obsolete. The rest need to be fixed.

1996 After hearing Sidon's Y2K bomb scenario, the board allocates \$5 million. Sidon hires Ernst & Young to help. The goal: to change as few dates as possible so that all the important ones get fixed.

1997 The company starts walling off entire sections of data processing while they're under repair so that new data isn't entered into old, flawed programs. The early fixes finish on schedule.

1997 People in the company whose systems are deemed noncritical start hearing that two-digit dates in their programs will not be converted to four-digit ones. Complaints start streaming in.

FEBRUARY, 1998 While working on the crucial claims system, programmers find that one of their shortcuts throws computers for a loop. The upshot: more work on an ever-tighter schedule.

MARCH, 1998 Three of the 10 core sections, or clusters, are fixed. The programmers expect that the remaining seven will be done by June, leaving more than a year for testing.

special, Y2K-compliant upgrades. "We've shut some of those vendors down," Sidon snorts.

After the initial winnowing, Sidon found he had 9,000 programs to revamp. In October, 1995, he went to top management and the board for the first time and explained the problem. It was an easy sell, he says, and he was handed

an initial budget of \$5 million. That small change today, when demand for expert Y2K programmers far exceeds supply. But in 1995, the Y2K service niche was just taking shape and consultants were hungry for experience in a promising new market.

Sidon got in touch with William Ruckle, managing director of Ernst & Young's nascent Year 2000 business. Ruckle's group was just finalizing plans for a 12-person software "factory" in Costa Mesa, Calif. At the same time, E&Y was negotiating a joint venture with an Indian contractor, the software arm of the giant Tata Group. The backup greatly eased the anxiety of customers such as Sidon. When the Y2K crunch hit, Ruckle explained, E&Y would be able to bounce terabytes of client data off satellites to programmers in multiple time zones. That way, E&Y would be able to fix faulty dates around the world and around the clock.

Ruckle took on Mutual as his first customer, offering to handle the bulk of Sidon's business in return for most of Mutual's budgeted \$5 million. That's about one-third what he would charge for a similar contract today. "It's the one we learned on," he explains.

After that, Sidon and his team performed the digital equivalent of brain surgery on Mutual's systems. Sidon and Ruckle began by dividing the company's systems into seven clusters, including workers' compensation cases, prescription drugs, and the most crucial one, the claims system. One by one, the team isolated the clusters and determined which programs and files to fix.

SAFE ZONE. Along the way, the two companies used myriad work-around schemes to safeguard programs and data without actually changing any dates. One is a well-known technique called a "sliding window," in which a computer is instructed to interpret an ambiguous two-digit date from 00 to 59, say, as 2000 to 2059. Currently, Mutual has applied the sliding window to about 80% of its date fixes.

Wherever two-digit dates must be replaced with four-digit ones, Mutual ships the whole software cluster out to Costa Mesa with explicit directions on what needs to be fixed. While under repair, that portion of the company enters a state called "freeze." People can still call up needed information. But they can only enter new information once a week or at the end of the entire process, depending on the depth of the freeze. It's a huge inconvenience. But it assures that no one unwittingly enters a program with a two-digit date, there

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by contaminating the cluster and spoiling perhaps thousands of hours of work.

After the fixed files return from California, the Mutual team and its E&Y assistants begin testing—a process that soaks up 45% of total remediation time. Finally, each repaired cluster is removed from freeze and placed into a clean area of the mainframe, called a “library.” This is segregated from the dirty library, where the two-digit files are still awaiting their fix. And woe to the employee who absentmindedly shuttles a dirty file into the clean library. “It’s a danger that we face—making sure that what gets renovated stays renovated,” says Sidon. Today, three of seven clusters reside in the clean library. Sidon intends to fix the remainder by June, so that Medical Mutual can close the books on 1998 with the new system—and make sure that it works.

FALSE HOPE. But if this sounds like a tidy finish, it’s not, as Mary Libens can testify. Take the sliding window. Libens originally planned to use this shortcut to deal with two-digit dates on electronic files that are used to track annual deductibles on claims. Since nothing in these files other than birthdates refers back as far as 1950, the team wrote a program that instructed computers to simply interpret all year dates up to 50 as postmillennial.

This solution almost worked. Programmers who tested it in Costa Mesa said the computers were no longer confused about which century the files addressed. But there was a different, unexpected snag: Whenever the computers bumped into the number 00, they would assume that they had reached the bottom of the deductible file. “There was no way to code around it,” says Libens. If they let it go, the computer could easily make an incorrect payment, by assuming, for example, that the deductible hadn’t been paid, when in fact it had been. The program had to be scrapped, and Libens is back to inserting four-digit dates in every file.

Libens perseveres, because she knows Mutual will make it through. But what of the large companies that are just getting started? In a recent survey of 450 businesses in North America, the Information Technology Assn. in Arlington, Va., found that 45% of them are still studying their systems and have yet to start fixing them. A year from now, they’ll begin hitting the same kinds of hitches and delays that Mutual has been living with for four years. It’s inevitable. It’s software. To one and to all... Godspeed.

By Stephen Baker in Cleveland

**KENNARD:
NO MORE
“BLAME GAME”**



TELECOMMUNICATIONS

LESS SOUND AND FURY AT THE FCC

New head Bill Kennard plays telecom peacemaker

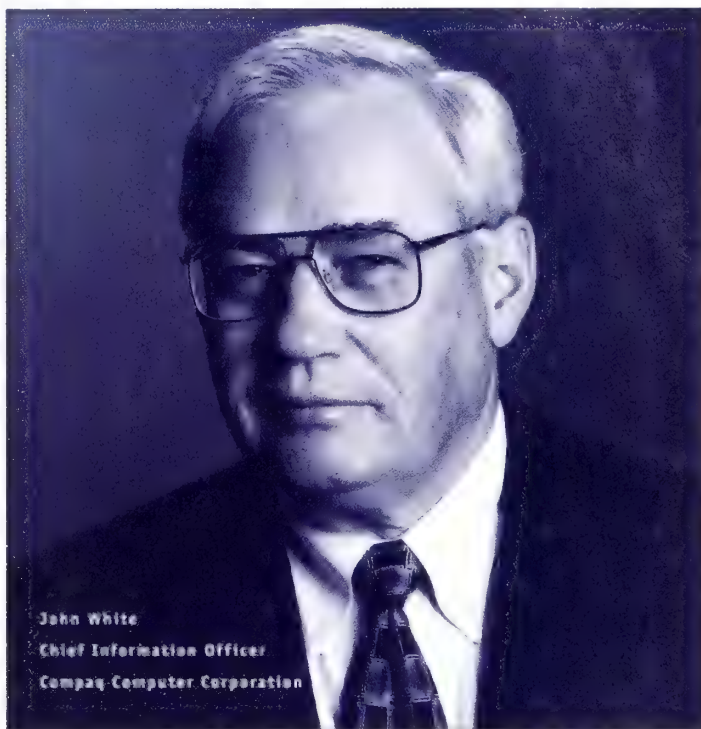
When William E. Kennard had his first get-acquainted meeting with powerful House Democrat John D. Dingell (D-Mich.) on Feb. 12, Dingell wasted no time in criticizing the new chairman of the Federal Communications Commission and his agency for a long list of sins, including not allowing the Baby Bells into the long-distance business. “It was the verbal equivalent of a horsewhipping,” says Kennard. Citing what he considered the agency’s policy missteps, Dingell more recently told the National Association of Broadcasters that the FCC chief “may be a few affiliates short of a network.”

Some 100 days after Bill Kennard took over as FCC chief, the laid-back

41-year-old Californian is squarely on the hot seat. He faces vein-popping pressure from Congress, industry, and the states—all steamed that two years after the Telecommunications Act of 1996, the law designed to promote competition has yet to bear fruit. Worse, he has stumbled politically—in one case by not notifying Senate Commerce Committee Chairman John McCain (R-Ariz.) of a White House initiative to give political candidates free airtime.

Now Kennard, the FCC’s former general counsel and its first African-American chairman, needs to regain momentum just as the commission faces perhaps the toughest challenges in its history. “The fights we’ve seen so far are hard,” says Anne K. Bingaman, se-

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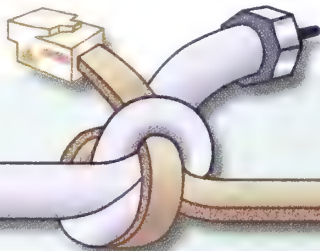
Instead of fighting fire with fire, though, Kennard is playing the peacemaker. While his predecessor, Reed E. Hundt, frequently warred with state regulators, Kennard has gone out of his way to work with them—and even made a point of giving his first speech as chairman to their trade group. That "was a real

the principal, Robert returned daily and eventually was accepted. Robert Kennard later founded the largest African-American architecture firm in Los Angeles. Says the younger Kennard: "You have to have your own inner compass and know where you want to go."

To find his way at the FCC, Kennard

sues. "Powell is a real force to be reckoned with," says Kennard's former law partner Lawrence R. Sidman, a telecom lobbyist.

Both men downplay the prospect of a clash. Powell says his paper was designed to advance discussion on a critical issue. It "was intended to encourage companies and regulators to get back to the table and redouble their efforts," he says. For Kennard's part, he notes that he suggested the same policy months earlier: "I'm more than happy to give other commissioners credit as long as



UNSNARLING THE FCC'S PROBLEMS

PHONE COMPETITION The FCC is taking heat for not making telecom deregulation happen faster. Kennard must now push the Baby Bells to open their local markets more quickly while resisting pressure to let the Bells into the long-distance business right away.

UNIVERSAL SERVICE Kennard is caught between farm-state Senators, who want to keep subsidies for rural and needy customers, and Vice-President Al Gore, who wants to use the money to fund schools' Net access.

CABLE RATES Despite opposition from cable operators, he must keep a lid on rates, even as the FCC's regulatory authority expires in March, 1999.

DIGITAL TV The FCC must accelerate the adoption of digital TV even as broadcasters drag their feet and complain that the new equipment is too pricey.

will have to overcome huge obstacles. Two years after the 1996 act, local phone competition is still just a promise for the vast majority of consumers. In the cable industry, lawmakers want the FCC to keep a lid on rising rates without extending a rate-regulation law that expires next year. And broadcasters are dragging their feet on the transition to digital television. "I can't remember a new chairman with the depth of problems he has to deal with," says Robert T. Blau, vice-president of Atlanta-based BellSouth Corp.

Another potential snag: rivalry from up-and-coming Republican Commissioner Michael K. Powell, who is the son of General Colin L. Powell. In January, the younger Powell took the unusual step of issuing his own paper detailing how the FCC can help the Bells with their as yet unsuccessful applications to enter the long-distance market. With that kind of initiative, Powell could grab the leadership role on key policy is-

the bottom line is consistent with my agenda. I reject the notion that the other commissioners must live in fear of the chairman."

Such confidence is bolstered by the fact that Kennard has had a stellar Washington career. As former FCC general counsel and a dealmaker before that at the heavyweight D.C. law firm of Verner, Liipfert, Bernhard, McPherson & Hand, he was known for his ability to craft a consensus in contentious situations.

As Kennard grapples with the challenges of leadership, he has even less time for favorite pursuits with his friends and family. Returning home by 10 p.m. means he had a "slow day at the office," says his wife of 1

years, Deborah D. Kennedy, an attorney for Mobil Corp. whom he met while both were at Yale. When he can, Kennard relaxes by fishing for small-mouth bass in the Shenandoah Valley.

Kennard won't have much time for angling while he's at the FCC. Besides completing the work left over from Hundt's tenure, Kennard wants to add his own imprint by "infusing [my agenda with opportunities] for minorities, women, and the disabled. That's an objective he has pursued throughout his career—he has provided legal advice to black-owned companies and done *pro bono* work for homeless youth. "We need to make sure the telecommunications revolution brings us together as a country," he says. That's a tall order. But in this era of rancor, Kennard will make a contribution just by forging peace among the titans battling at the FCC.

By Catherine Yang
in Washington

turning point," says Jolynn Barry Butler, president of the state regulators' association. After the speech, so many state officials wanted to chat with the new chairman that original plans for a small dinner party grew to a table of 20. "Our challenge is to get out of the blame game," says Kennard, a Yale Law School grad. "We need to get everybody invested in the success of the Telecom Act."

That attitude comes as no surprise, given Kennard's role model. As a teenager, he had a complete set of Martin Luther King Jr.'s speeches on records that he would listen to repeatedly. Now, he's using many of King's values of cooperation at the FCC. "In another 20 years, all the noise will be forgotten and we'll all be judged by what we did," he says. "I'm confident that I'll be on the right side of history."

Kennard is starting to make his mark with a down-to-earth attitude that puts him in sharp contrast with the imperious Hundt. At the FCC, he arranged one- to two-hour "Bible readings" of the Telecom Act so he could get others' opinions on the often-abstruse law. And he has begun a regular coffee klatch with the four other commissioners after formal meetings.

"INNER COMPASS." Kennard's ability to work with differing views and backgrounds stems from his parents and from his childhood in the interracial Hollywood Hills. His mother grew up among Hispanic migrant workers and became a bilingual schoolteacher. When his father, Robert, was nine, his parents sent him to a nearby whites-only school instead of a black one farther away. Although he was harassed by the kids and repeatedly denied admittance by

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Who among the
S&P 500 has
the most on
the ball? Our
growth rankings
offer surprising
insights into
America's most
closely watched
companies

THE
BUSINESS
WEEK

50

In a period marred by slowing computer sales growth, allegations of antitrust Capitol Hill hostility, and even a pie in the face, there is one thing William H. Gates III hasn't had to worry about: corporate performance. Whether you think Microsoft Corp. anticompetitive or simply ultracompetitive, under Gates's leadership it has racked up a record of annual profit and revenue increases that is the envy of Corporate America. "We've been cruising for 22 years," says Gates, Microsoft's chairman.

It sure looks like full speed ahead to the rest of us. With earnings galloping ahead 57% last year, the Redmond (Wash.) software giant turned in an eye-popping 76.3% gain for shareholders. That was enough for Microsoft to knock chipmaker Intel Corp. out of the No. 1 spot in BUSINESS WEEK's second annual performance ranking of the 500 companies in the Standard & Poor's index. And getting there was no easy ride: To earn the highest honors, Microsoft blew past staunch competition from such top 10 sizzlers as Dell Com-

IN THIS REPORT:

76 THE TOP 50 performers cut a wide swath across Corporate America

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er, Cisco Systems, credit-card dynamo MBNA, and Morgan Stanley Dean Witter & Co.

ask Gates what's behind the success that has kept his company several steps ahead of such a crowd, and he credits being the right business at the right time. "It's the Information Age, and we're giving people great tools for getting at and handling information," he says. There's certainly more to it than that. Thanks to the legendary aggressiveness Gates fosters, 90% of the 80 million PCs shipped last year were loaded with one version or another of Microsoft's Windows operating systems. What's really impressive about Microsoft is its obsession with efficiency and gradually improving products.

From every dollar in sales, Microsoft pulls out 29.7¢ in profits—margin that grew by 13% over the year before. That's almost three times the average for its industry, and better than all but a few other companies in all the 500. Moreover, between fiscal 1995 and 1997, the company's share of revenues going into research and development climbed from 14% to 17%—without denting profits. "How do we do it? We watch costs like a hawk," says Microsoft President and Chief Operating Officer Robert J. Herbold. Given the phenomenal growth that the PC industry has seen

ST MERS

- 1 MICROSOFT
- 2 DELL COMPUTER
- 3 CISCO SYSTEMS
- 4 INTEL
- 5 COMPAQ COMPUTER
- 6 MBNA
- 7 TELLABS
- 8 EMC
- 9 COMPUTER ASSOCIATES INT.
- 10 MORGAN STANLEY
DEAN WITTER
- 11 SCHERING-PLOUGH
- 12 PFIZER
- 13 APPLIED MATERIALS
- 14 US AIRWAYS GROUP
- 15 MERCK
- 16 TRAVELERS GROUP
- 17 GAP
- 18 SCHLUMBERGER
- 19 MERRILL LYNCH
- 20 SUN MICROSYSTEMS
- 21 TJX
- 22 BRISTOL-MYERS SQUIBB
- 23 HBO
- 24 CHASE MANHATTAN
- 25 CONSECO
- 26 MGIC INVESTMENT
- 27 COUNTRYWIDE CREDIT
INDUSTRIES
- 28 GUIDANT
- 29 PACCAR
- 30 OMNICOM GROUP
- 31 NORTHERN TELECOM
- 32 CHARLES SCHWAB
- 33 PROGRESSIVE
- 34 SUNAMERICA
- 35 STATE STREET
- 36 LEHMAN BROTHERS
HOLDINGS
- 37 PARAMETRIC TECHNOLOGY
- 38 GILLETTE
- 39 CORESTATES FINANCIAL
- 40 NORWEST
- 41 GENERAL ELECTRIC
- 42 FANNIE MAE
- 43 HALLIBURTON
- 44 HOME DEPOT
- 45 FREDDIE MAC
- 46 HEALTHSOUTH
- 47 CLEAR CHANNEL
COMMUNICATIONS
- 48 RITE AID
- 49 ALLSTATE
- 50 NATIONSBANK

In recent years, it's no surprise that Microsoft would top BUSINESS WEEK's ranking of corporate performance. It moved up a notch when last year's winner, Intel, slipped down to No. 4.

High-tech leaders Dell, Cisco, and Compaq Computer round out the first five spots. But if it helped to be in a fast-growing high-tech field, it was hardly necessary: The top performers cut a wide swath across Corporate America. This year's BUSINESS WEEK 50—our exclusive ranking of best overall performers among the S&P 500 companies—includes everyone from drug giant Pfizer Inc. and long-haul truckmaker PACCAR Inc. to oil services giant Schlumberger Ltd. and clothing retailer Gap Inc.

DYNAMISM. That's because we developed our Performance Rankings to reflect more than just size by sales or market capitalization. Instead, we created a ranking in which the best in each industry—and the best overall—truly shine through. Unlike more traditional lists, in which big is defined as best, we place a premium on the dynamism and growth that successful companies must cultivate to survive.

After all, in today's hugely competitive global economy,

what really matters? For small companies and their large brethren alike, it's the ability to grow—to keep pushing sales, piling up earnings, and, most important, to continue rewarding shareholders with ever-higher returns. "Great companies try to grow, to be innovators forever," says Charles Lucier, a consultant with Booz, Allen & Hamilton Inc. "It's hard to sustain."

For proof, look no further than this year's Performance Rankings and the BW 50. Like the American economy they reflect, our rankings provide a dynamic canvas against which brutal competitive realities stand out; it's a fast-moving portrait in which rising stars push aside companies that have stalled out. Although they won't look like many other best-lists you've seen, the Performance Rankings are likely to provide far more insight into which companies really soar above the crowd.

Certainly, that was the case with last year's BW 50. As a group, they continued to outperform: Over the 12 months ended March 13, shares of the BW 50 companies rose a head

BusinessWeek ONLINE Additional data from S&P's Personal Wealth and S&P's Compustat are available for the BW 50 and all other companies in these tables at www.businessweek.com

HOW WE PICKED THE CREAM OF THE CROP

What makes for a top corporate performer? That's what BUSINESS WEEK set out to discover last year when we introduced our all-new Performance Rankings and its centerpiece, the BUSINESS WEEK 50—the best overall performers among the S&P 500 companies. Our aim was to go beyond static lists that rank companies by sheer size or market capitalization. Instead, we created a dynamic, growth-oriented measure that would truly reflect—and reward—companies that consistently perform better than their peers.

So how did we calculate our Performance Rankings? We began with two of the most important factors investors use to judge performance: top-line revenue growth and earnings growth. We then added total returns, a key measure of how well management is performing for shareholders. Since it is much harder to sustain growth than sprint for a few quarters, we tallied all three of those crucial rates over both one- and three-year time spans. Finally, we added two important indicators of the returns management earns from its assets: net margins and return on equity, both for one year. After all, what good is growth if it doesn't pay off financially?

Using those criteria, we evaluated each of the companies in the closely watched Standard & Poor's 500-stock

index. S&P is owned by The McGraw-Hill Companies, which also owns BUSINESS WEEK. Why the S&P 500? Because it is a universally accepted measure for stock performance, both on Wall Street and among small investors. Its 500 companies together



comprise 70% of the market value of U.S. stocks.

The results give an in-depth look at how these companies really stack up against one another. Who had the best—or worst—three-year shareholder return among the 500? The best net margins? Answers to those

questions and more can be found in the tables throughout this package.

But that's only a start. We also graded the 500 companies on each of the eight criteria, based on how well each performed against other companies in the index. For each measure, the top 20% of companies earned an A, the next 20% got a B, and so on down to the F's in the bottom 20%. The handful of S&P companies for which data was not available got incompletes.

Finally, to get our overall Performance Ranking of the 500—and select the elite that make up each year's BW 50—we averaged together the individual rankings each company received for the different criteria. Then, to recognize that it's much easier for small companies to score big percentage gains than it is for big companies, we weighted them by sales volume.

The result is our overall Performance Rankings, which starts on page 91. The same criteria form the basis for each company's ranking within its sector; our Industry Rankings tables begin on page 123. Together, they form an annual corporate report card. At the top are the stars of the dean's list. At the bottom are the laggards: those that would be well advised to hit the books a little harder this year.

By Dan Beucke in New York

TOTAL RETURN *The best and worst in shareholder returns*

TOP TEN (ONE-YEAR)		BOTTOM TEN (ONE-YEAR)		TOP TEN (THREE-YEAR)		BOTTOM TEN (THREE-YEAR)	
PERCENT INCREASE		PERCENT DECREASE		PERCENT INCREASE		PERCENT DECREASE	
DELL COMPUTER	298.9%	FREEPORT	-53.9%	DELL COMPUTER	2,596.4%	SILICON GRAPHICS	-56.5%
US AIRWAYS GROUP	216.6	McMORAN COPPER & GOLD		US AIRWAYS GROUP	977.7	STONE CONTAINER	-49.0
NAVISTAR INTL.	215.6	SEAGATE TECH.	-51.9	GUIDANT	708.6	NOVELL	-48.3
UNISYS	164.8	JOHN H. HARLAND	-49.8	CLEAR CHANNEL	536.5	DSC	-45.5
NACCO INDUSTRIES	142.5	INCO	-49.3	COMMUNICATIONS		COMMUNICATIONS	
TELE-COMMUNICATIONS	133.7	CABLETRON SYSTEMS	-47.0	TJX	509.2	APPLE COMPUTER	-39.5
GUIDANT	117.6	NIKE	-40.3	SUN MICROSYSTEMS	495.3	BATTLE MTN. GOLD	-35.8
MAYTAG	113.1	PLACER DOME	-39.0	CISCO SYSTEMS	485.6	PLACER DOME	-34.1
EMC	109.7	GREEN TREE FINANCIAL	-38.7	HBO	465.6	HOMESTAKE MINING	-33.2
PACCAR	109.4	HOMESTAKE MINING	-38.3	MICROSOFT	438.1	CYPRUS AMAX	-32.8
		TUPPERWARE	-38.2	CONSECO	434.8	MINERALS	
						BETHLEHEM STEEL	-32.5

DATA: STANDARD & POOR'S COMPUSTAT, A DIVISION OF THE MCGRAW-HILL COMPANIES

, handily beating both the 34.7% turned in by the S&P and the 24% gains tallied by the Dow Jones Industrial Average. With a stunning 260% price gain, Dell was the top performer, followed by EMC with 115%, and Schering-Plough with 109.4%. But they weren't the only overachievers: In all, 31 of the top 50 beat the S&P-500 index.

MARKETING. So what made the best stand out? While no two companies made it onto the BW 50 for exactly the same reasons, distinct trends emerge that go well beyond one industry or a star manager. The enormous wave of mergers and acquisitions now sweeping Corporate America left its mark. From Dean Witter's marriage to Morgan Stanley, to the clothing giant TJX Companies' purchase of former rival Marshall Field's Inc., more than a dozen of this year's stars turned to acquisitions to fuel their rapid-fire growth.

Elsewhere, there are trends to note. General Electric Co. and Microsoft demonstrate that the drive for corporate efficiency is no thing of the past. The steady success of the drug makers exemplify the unbeatable combination of innovative product and aggressive marketing. And remember the customer is always right? For example, manufacturer Applied Materials Inc.

little-known EMC Corp., a maker of computer storage systems, prove that old saw, too, is alive and well.

How did BUSINESS WEEK find the stars that best exploit the trends? To sort out the best performers among Corporate America, we employed a range of key measurements that investors and managers alike use to judge operating performance. Starting with the 500 companies in the S&P index as our universe, we compared the one- and three-year record each has turned in for sales growth, net income growth, and total shareholder returns. We also added at last year's profit margin and return on equity. (For a detailed look at how we compile the rankings, see page 78.)

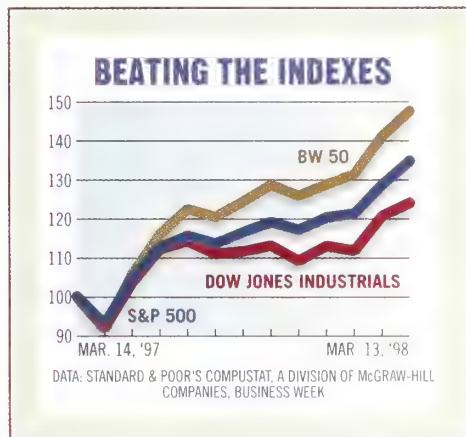
Add it all up, and the resulting rankings gave us the crème de la crème—the BW 50. Over the last three years, these companies have bested rivals. Those Performance Rankings, which include a detailed look at how each company fared on individual criteria, start on page 91.

Of course, it's also important to compare companies with industry peers. In some cases, superior management teams have bucked dismal industry growth rates to post supercharged overall performance. That's why we've also included extensive Industry Rankings, which include the actual growth rates upon which our Performance Rankings are

based. Those tables also include sales and profit figures, as well as such shareholder information as recent share price, price-earnings ratio, yield, and earnings per share. Industry Rankings begin on page 123. An alphabetical index of the S&P 500, with company ranking by market value, sales, and profits, begins on page 150.

Those tables provide a look at what it takes to succeed in Corporate America—and how hard it is to stay on top. Of the top performers on last year's BUSINESS WEEK 50, fully half fell off and were replaced by new companies this year. In part, that's because the S&P is itself a changing universe; the composition of the index changes from year to year. In 1997, for example, S&P replaced 29 companies in the index—and 10 of the newcomers shot straight to the head of the class. Among them: advertising giant Omnicom Group, Wall Street powerhouse Lehman Brothers Holdings, and HBO & Co., which sells health-care information systems.

But just as important, other entrants emerged that reflect the changing fortunes of America's corporations. Thanks largely to a global exploration boom, oil services giants Schlumberger and Halliburton Co. rocketed onto this year's top 50. The ability of Home Depot Inc., the fixer-upper's paradise, to keep churning out strong and steady growth as it enters new domestic markets won it a spot for the first



SALES *The best and worst in sales performance*

TOP TEN (ONE-YEAR)

PERCENT INCREASE

CLEAR CHANNEL COM.	98%
RITE AID	89
CONSECO	82
HOUSTON INDUSTRIES	68
PACIFICORP	65
WORLDCOM	64
PG&E	60
AIRTOUCH COMMUNS.	60
DELL COMPUTER	59
DOMINION RESOURCES	54

BOTTOM TEN (ONE-YEAR)

PERCENT DECREASE

NOVELL	-33%
APPLE COMPUTER	-26
MOBIL	-19
COASTAL	-19
BATTLE MTN. GOLD	-19
TANDY	-15
FRUIT OF THE LOOM	-13
KERR-McGEE	-11
HOMESTAKE MINING	-11
TUPPERWARE	-10

TOP TEN (THREE-YEAR)

AVERAGE ANNUAL INCREASE

WASHINGTON MUTUAL	83.6%
CENDANT	75.0
CISCO SYSTEMS	70.0
DUKE ENERGY	62.2
HILTON HOTELS	61.5
CLEAR CHANNEL COM.	57.1
KLA-TENCOR	57.1
CONSOLIDATED STORES	53.4
DELL COMPUTER	51.9
TENET HEALTHCARE	50.3

BOTTOM TEN (THREE-YEAR)

AVERAGE ANNUAL DECREASE

NOVELL	-24.9
RALSTON PURINA	-19.3
GREAT LAKES CHEM.	-17.5
APPLE COMPUTER	-13.0
HERCULES	-13.0
PEPSICO	-12.4
AT&T	-10.8
MORTON INTL.	-10.5
ROCKWELL INTL.	-10.4
LINCOLN NATL.	-9.8

time. The tremendous turnaround at US Airways helped lift it to the No. 2 spot in total returns—and 14 overall.

Equally interesting, of course, are those that fell off. Last year's No. 50, hospital company Columbia/HCA Healthcare Corp., slid to No. 457 as it took a big charge against earnings amid a government investigation of its billing practices, which sent profits down 88% and shareholder returns tumbling 35%. Problems in Asia flattened once mighty Nike Inc., which dropped from No. 7 to No. 64. Coca-Cola Co., which gets 80% of its sales and earnings overseas, was also hit hard by the persistently strong dollar. With sales growth nearly halted, it slipped from No. 25 to No. 119.

So who came out ahead? Thanks to the combination of a still strong bull market and a global M&A boom—not to mention a run of dealmaking by the industry's main players—brokerages and other nonbank financial companies grabbed 13 spots on the BW 50, the most of any industry. With investment banking and underwriting fees soaring, Merrill Lynch & Co., No. 19, stood out: It earned \$30 million on the \$31 billion merger of Bell Atlantic Corp. and Nynex alone.

ANOMALIES. Thanks to the Internet, worldwide growth in business computers, and an increasing PC presence in homes, makers of computers, software, and other office equipment hogged nine spots on the list. Intel took one more.

Yet if being in a hot industry helped, it was rarely enough by itself to lift laggards to the top. Intel's ability to boost the performance of its chips, even as it cuts manufacturing costs, may keep it near the top, but rival Advanced Micro Devices Inc. weighs in at a lowly No. 474. Despite having a microprocessor that is challenging Intel's dominant Pentium line, AMD lost money because it couldn't lick production problems. And despite a boom in credit that has buoyed much of the rest of the financial-services industry, Green Tree Financial Corp. fell victim to its own aggressive accounting. No. 19 last year, it slipped to No. 150 as its

stock and earnings melted in the wake of a \$190 million write-down.

Much like last year, the 1998 BW 50 crop contained its share of surprise newcomers. The list includes some dealmakers you probably didn't know existed, from truckmaker PACCAR to mortgage banker Countrywide Credit Industries Inc. (page 82).

Like all such lists, the BUSINESS WEEK ranking has anomalies. One thing to keep in mind as you check out the table: Companies recovering from a down year can show a big jump in net income that makes them look better than they really are. Take Humana Inc., the big health maintenance organization. It tops our one-year profit growth list with a 1,342% increase. Looks impressive, until you consider that the company's 1996 earnings were almost completely wiped out by a \$130 million charge—providing a very low base on which to improve. That's why we've included three-year performance numbers as well—and there is definitely one case where the longer view

is invaluable: Humana's average profit change over three years is -24.5%.

A shift in corporate strategy can also alter the ranking. Companies that went public or were spun off less than three years ago don't register on the BW 50 radar screen, because they simply don't have enough data yet to allow for fair comparisons. AT&T spin-off Lucent Technologies Inc., for example, hasn't been independent long enough to be judged on its three-year stock performance. Meanwhile, companies such as AT&T that do the spin-offs sometimes slide down the list as sales and earnings shrink.

Taken as a whole, however, the Performance Ranking provides valuable insight into the forces which are transforming Corporate America. You don't have to go far down the list before hitting one of the biggest: Fueled by stiffening global competition and consolidation at home and abroad, many U.S. companies are using mergers to ratchet up the

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The mergers-and-acquisitions boom is one of the biggest forces changing Corporate America



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as current
as your
software.**

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Kelly Staff Leasing

The Wallace Law
Registry

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Resources

Kelly Temporary
Services

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growth. After racking up deals worth a record \$912 billion in 1997, an additional \$196.2 billion worth have already been announced this year. "We see no loss of momentum," says Jack Levy, head of M&A at Merrill Lynch. "CEOs and boards today are so keenly focused on establishing a No. 1 or No. 2 position in their industry."

M&A BOOST. That was certainly the case with Morgan Stanley's \$10.6 billion combination with Dean Witter, Discover & Co. The desire to improve distribution was the main draw for the deal, which pushed the company up into the No. 10 slot. Not only can initial public offerings underwritten by Morgan Stanley now be sold through both firms' brokers, but

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50

the promise of a broader customer base helped the company increase its share of worldwide equities underwritings, from 7.3% to 9.4% since the deal closed. "It gave us incredible revenue growth," says CEO Philip J. Purcell. Indeed, sales grew 22% last year, capping

strong three-year streak in which investors watched total returns rise 262.5%.

For many of the smaller firms in the S&P 500, mergers have also proven a quick way to bolster product lines. Take Clear Channel Communications Inc., a little-known owner of radio boards, radio stations, and TV channels which made \$3.5 billion in acquisitions last year. The crowning touch was its \$1.1 billion purchase of Eller Media, which moved the budding media

THE NIMBLE NEW LEADERS OF THE PACK

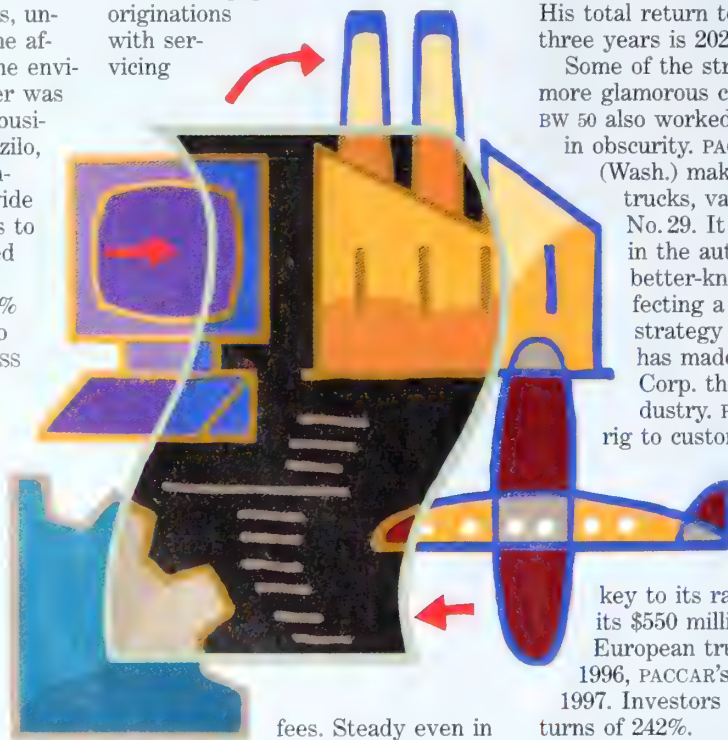
Unless you're one of the millions of Americans who recently bought or refinanced a house, you've probably never heard of Countrywide Credit Industries Inc. Although the largest independent mortgage broker in the U.S., Countrywide has only 5% of the market.

But in 1997, 5% was plenty. With interest rates near record lows, unemployment minimal, and home affordability at all-time highs, the environment for a mortgage broker was ideal. "In my 45 years in the business," says CEO Angelo R. Mozilo, "I have never seen an environment like this." Yet Countrywide is no one-year wonder. Thanks to sales growth that has averaged 24.6% annually over the past three years—and sizzling 42.8% earnings gains—it zoomed into the No. 27 spot on the BUSINESS WEEK 50 after being added to the Standard & Poor's 500-stock index last year.

Countrywide is one of several names on this year's BW 50 that may be unfamiliar. Ever heard of Progressive Corp.? PACCAR Inc.? How about HBO & Co.? No, it's not the cable-TV channel—the Atlanta-based company provides information systems to the health-care industry. The S&P 500 may list the most closely watched companies in America, but by focusing on three separate growth measures, our Performance Rankings scooped up these and other little-known gems.

They all have found some way to push to the front of the pack. Some, like HBO, have tailored products to their customers better than their rivals. Others, like Progressive, excel

at service. And when markets shift, many of the newcomers don't wait to get squashed. Since 1994, when a crushing price war broke out in mortgages, Countrywide has moved to minimize the impact of rate changes on its revenue stream. Now, the Pasadena (Calif.) company balances mortgage originations with servicing



fees. Steady even in times of rising rates and heavy price competition, fees now make up half of its revenues.

Often these unsung performers have had little choice but to innovate. That was the case in the early 1990s for auto insurer Progressive of Mayfield Village, Ohio. Then specializing in high-margin policies for motorcycle riders and other risky drivers, it was forced by growing

competition from mainline property and casualty insurers to move into traditional auto insurance for a broad base of drivers. Peter B. Lewis, who has been CEO for 33 years, figured he could set Progressive apart by offering the highest service levels possible, such as 24-hour, seven-day-a-week service by phone. It worked: His total return to shareholders over three years is 202%.

Some of the strategies that landed more glamorous companies atop the BW 50 also worked for those laboring in obscurity. PACCAR, a Bellevue (Wash.) maker of long-haul trucks, vaulted 328 places, to No. 29. It snatched the lead in the auto industry from its better-known rivals by perfecting a lean manufacturing strategy similar to one that has made Dell Computer Corp. the star of the PC industry. PACCAR builds each rig to customer specifications, keeping inventories low and margins high. Acquisitions have also been

key to its rapid rise. Thanks to its \$550 million purchase of a European trucking outfit in late 1996, PACCAR's sales grew 47% in 1997. Investors saw three-year returns of 242%.

Trucks, hospital equipment, insurance—it's hardly glamorous. But as our unknown dynamos have proven, these businesses can be highly profitable. And when it comes to breaking onto the BW 50, it's more important to move fast than to move in fast circles.

By Nanette Byrnes in New York, with Kathleen Morris in Los Angeles, Stephanie Anderson Forest in Dallas, and bureau reports

MOST PEOPLE THINK OF US AS AN EXCELLENT DOMESTIC AIRLINE. WE HATE THAT.

For the record, we fly to more than 190 destinations in 32 countries worldwide. In fact, we're one of the largest carriers to Latin America. With flights to over 30 cities throughout Mexico, Central and South America and the Caribbean, Continental can easily get you to São Paulo, Rio de Janeiro, Panama City, Mexico City, Caracas and more. In addition, bilingual flight attendants, Latin American cuisine and OnePass® miles are available on all flights.

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empire into the billboard market. The company's ability to offer packages of radio and billboard advertising has now become a key competitive advantage, says CEO L. Lowry Mays. It has certainly paid off: Clear Channel's resulting 98% sales spurt was the biggest one-year gain of the entire S&P 500.

INTERNAL ENGINE. But not every company on the BW 50 went looking beyond its own doorstep for prospects. Many others have proven masters at generating growth internally. Perhaps none exemplifies that better than No. 2-ranked Dell, where ultra-efficient manufacturing underpins its ability to move rapidly into new markets on its own. Founder Michael S. Dell supplies custom-made machines directly to buyers, stripping out the costs of inventory and retail distribution. Dell's skimpy one week of inventory—just one-tenth that of rivals—gives the company a 10% to 15% cost advantage over rivals. The fast sales growth that results has allowed



But that single-minded focus—and the intense drive it takes to stay on top—isn't limited to those in the high-tech world. It permeates the ranks of the BW 50, perhaps nowhere more so than at No. 41-ranked General Electric Co. CEO John F. Welch, 62, may be in his 17th year at the helm of the conglomerate, but he's hardly counting his days until retirement. Indeed, the legendary CEO remains as intense as ever in his push for ever higher growth. The result: Though GE, with \$91 billion in sales, is more than twice as big as the next largest company in the BW 50, it's growing faster than many a sprightly small firm. Sales rose an impressive 15% last year as net income jumped 13%. Shareholders have reaped the rewards—a 203.4% return over the last three years.

In part, GE's surprising agility stems from a shift the company has made to take ever more advantage of global markets and to move away from manufacturing in favor of higher-margined services. But no matter how big it gets, Welch also makes sure that GE execs continue to sweat the small stuff. Over the past two years, GE has become immersed in a companywide quality program called Six Sigma, by reducing manufacturing and product defects. Welch figures GE can save hundreds of millions in costs. "Six Sigma has spread like wildfire across the compa-

EARNINGS GROWTH *The best in profits growth*

TOP TEN (ONE-YEAR)

PERCENT INCREASE

HUMANA	1342%
GOODYEAR TIRE & RUBBER	449
BALL	345
AETNA	339
US AIRWAYS GROUP	289
DELTA AIR LINES	275
COMPUTER ASSOCIATES INTL.	274
SCIENTIFIC-ATLANTA	220
NEW YORK TIMES	210
CONAGRA	199

TOP TEN (THREE-YEAR)

AVERAGE ANNUAL INCREASE

THOMAS & BETTS	264.1%
US AIRWAYS GROUP	193.1
ADOBE SYSTEMS	190.4
NORTHROP GRUMMAN	109.7
RAYCHEM	95.3
BOSTON SCIENTIFIC	87.9
HELMERICH & PAYNE	86.7
DELL COMPUTER	86.0
HEALTHSOUTH	85.9
AMR	84.9

DATA: STANDARD & POOR'S COMPUSTAT, A DIVISION OF THE MCGRAW-HILL COMPANIES

how to innovate outside of the lab. Having built up a potent sales force to serve up its own new drugs, it has leveraged its marketing skills by signing deals to help other companies sell promising new products. In so doing it ensures its margins remain stellar. Take its successful joint marketing venture with Warner-Lambert Co. for cholesterol reducer Lipitor. Developed by Warner-Lambert and introduced to the market in February, 1997, Lipitor is also sold by 1,200 Pfizer salespeople. Today, it has become the most successful drug introduction ever—and Pfizer gets a cut of the sales. "Our whole strategy has been growth through innovation," says CEO William C. Steere Jr. "Not just in research but innovation through clinical development and marketing activity."

Many of our superstars also got to the top by focusing intensely on meeting customer needs. That's the case at Gap Inc. The combination of marketing prowess with a never ending study of its customers has allowed the San Francisco-based clothing retailer to become one of three retailers to make it to this year's BW 50. Sure, the strength of America's shift to casual wear helped fuel the sales and earnings boom that has lifted Gap to No. 17. But CEO Michael S. Drexler has also been hugely effective at slicing the market with the company's Gap, Banana Republic, GapKids and Old Navy stores. By aiming the chains at different age and income groups, Gap has been able to attract a strong following for each. While the rest of the clothing store industry struggles with overcapacity, Gap keeps opening up new locations. Over the last three years, sales have grown at an average 20.4%.

Maybe it's not revolutionary that a retailer listens to its customers. But the success of No. 13-ranked Applied Materials is also founded on believing the customer is always right. The leading manufacturer of chipmaking equipment with market shares ranging from 30%

EARNINGS DECLINE

BOTTOM TEN

(TWELVE-MONTH LOSS)

MILLIONS OF DOLLARS

WASTE MANAGEMENT	-\$1274.2
QUAKER OATS	-930.9
APPLE COMPUTER	-878.0
UNISYS	-853.6
DOW JONES	-802.1
SARA LEE	-567.0
CHAMPION INTL.	-548.5
US WEST MEDIA GRP.	-480.0
STONE CONTAINER	-404.4
TELE-COMMUNICATIONS	-399.0

DATA: STANDARD & POOR'S COMPUSTAT, A DIVISION OF THE MCGRAW-HILL COMPANIES

Charles Schwab

to 60% in several key areas, it involves customers every step of the way in the development of new products.

A few years ago, when CEO James C. Morgan became interested in supplying systems that make computer flat-panel displays, his Japanese team was able to persuade Sharp Corp. and Toshiba Corp., long-term customers but archrivals, to share their knowledge of flat panels. That helped Applied Materials efficiently enter a whole new market, while rapidly giving the Japanese companies the equipment they needed. "That close a relationship—it's built over a long period of time," Morgan says.

SINGLE-MINDED DEVOTION. Those kinds of gains only come when a company knows its own markets and customers well—and focuses intently on them. That's why its no surprise that a single-minded devotion to core markets is another feature of many of our performance champions. Few demonstrate that better than Tellabs Inc. of Lisle, Ill., which moved up to No. 7 from No. 21. The maker of digital network-switching equipment decided years ago to concentrate on equipment that is used to direct data, video, and voice signals from one telephone company's lines to those of another. With pressure mounting on local phone companies to open their networks to competitors such as the long-distance carriers, Tellabs finds itself "in the sweet spot of the business," says CEO Michael J. Birck.

Tellabs' earlier decision to concentrate is now paying off in spades, as it holds off much larger rivals such as Northern Telecom Ltd. and Lucent. "We're much more specialized," says Birck. "Maybe that focus has given us a competitive advantage." It certainly seems so: Tellabs, with \$1.2 billion in sales, boosted profits a sizzling 124% last year, even as service providers such as MCI Communications Corp. and AT&T lost tens of millions of dollars. All told, the company has averaged annual profits hikes of 47.7% over the last three years, while shareholders rang up an eye-popping 364.4% return.

In a very different market, Charles Schwab Corp., No. 31, also demonstrates the gains to be reaped from seeing a growing market niche and positioning your company to take advantage of it. Throughout the long-running bull market,

NET MARGIN *The best and worst margins*

TOP TEN (1997)	PERCENT	BOTTOM TEN (1997)	PERCENT
MBIA	57.2%	ALZA	-56.2%
MGIC INVESTMENT	37.2	DOW JONES	-31.2
SUNAMERICA	34.5	HOMESTAKE MINING	-25.6
UST	31.3	PLACER DOME	-20.6
MICROSOFT	29.7	QUAKER OATS	-18.6
INTEL	27.7	FRUIT OF THE LOOM	-18.0
PARAMETRIC TECHNOLOGY	27.4	WASTE MGMT.	-13.9
AMGEN	26.8	APPLE COMPUTER	-13.4
COMPUTER ASSOCIATES INTL.	24.7	MALLINCKRODT	-13.0
MELLON BANK	23.6	NOVELL	-13.0

DATA: STANDARD & POOR'S COMPUSTAT, A DIVISION OF THE MCGRAW-HILL COMPANIES

Schwab has set itself up as the low-cost financial-service provider of choice for millions of Americans.

By offering everything from online trading and a funds supermarket to advice for befuddled investors, the discount broker has kept sales humming at a steady 30.8% a year since 1994. "Obviously we have had the wind at our back," says David S. Pottruck, Schwab's co-CEO. And if it shifts? Pottruck admits a sustained market decline will hurt Schwab's growth, but says it will adapt: "People are always going to want to manage their money and look to the future."

They won't be the only ones looking ahead. Indeed, for investors, as for some of this year's BW 50 stars, the future is already grown murky. With sub-\$1,000 PCs now driving growth in the computer market, stars such as Compaq and Intel will have their mettle tested in the year ahead. Intel

shocked Wall Street when it warned in March that first-quarter revenues would slip below those of a year earlier for the first time in a decade. The culprit: Those cheap PCs

leave no room for the \$250-plus microprocessors that have kept Intel's margins at their traditional sky-high levels. And with a glut of high-priced machines to unload at a discount, Compaq recently announced that 1998 profits will probably fall 25%.

Still, Compaq CEO Eckhard Pfeiffer insists the reversal is temporary. Promising to be on track by midyear, he's sticking to plans to double revenues by 2000. "We'll continue our aggressive market share strategy," he says.

Brave talk? Perhaps. In any case, it's inevitable that some big names will drop from the BW 50 ranks next year. So who will come out ahead a year from now? It's far too early to tell. Few could have predicted the fall of Coke, Nike a year ago, or the surprising rise of Clear Channel since. But armed with a wealth of information on the performance of the 500 most watched companies in America, investors can see which management teams have found their way to the winner's circle today.

By Nanette Byrnes with Amy Barrett in Philadelphia, Steve Hamm and Andy Reinhardt in San Mateo, Ga., and McWilliams in Houston, and bureau reports

RETURN ON EQUITY *The best and worst ROE*

TOP TEN (1997)	PERCENT	BOTTOM TEN (1997)	PERCENT
ORYX ENERGY	159.3%	TELE-COMMUNICATIONS	-995.5%
US AIRWAYS GROUP	155.0	QUAKER OATS	-347.1
AVON PRODUCTS	149.3	STONE CONTAINER	-95.7
UST	111.0	ALZA	-86.7
GENERAL MILLS	100.2	APPLE COMPUTER	-70.6
DELL COMPUTER	73.0	UNISYS	-62.8
CAMPBELL SOUP	62.5	DOW JONES	-47.7
COCA-COLA	56.7	FRUIT OF THE LOOM	-46.7
KELLOGG	56.5	MALLINCKRODT	-32.6
SCHERING-PLOUGH	53.4	HOMESTAKE MINING	-31.8

Excludes companies with negative equity.

DATA: STANDARD & POOR'S COMPUSTAT, A DIVISION OF THE MCGRAW-HILL COMPANIES

THE
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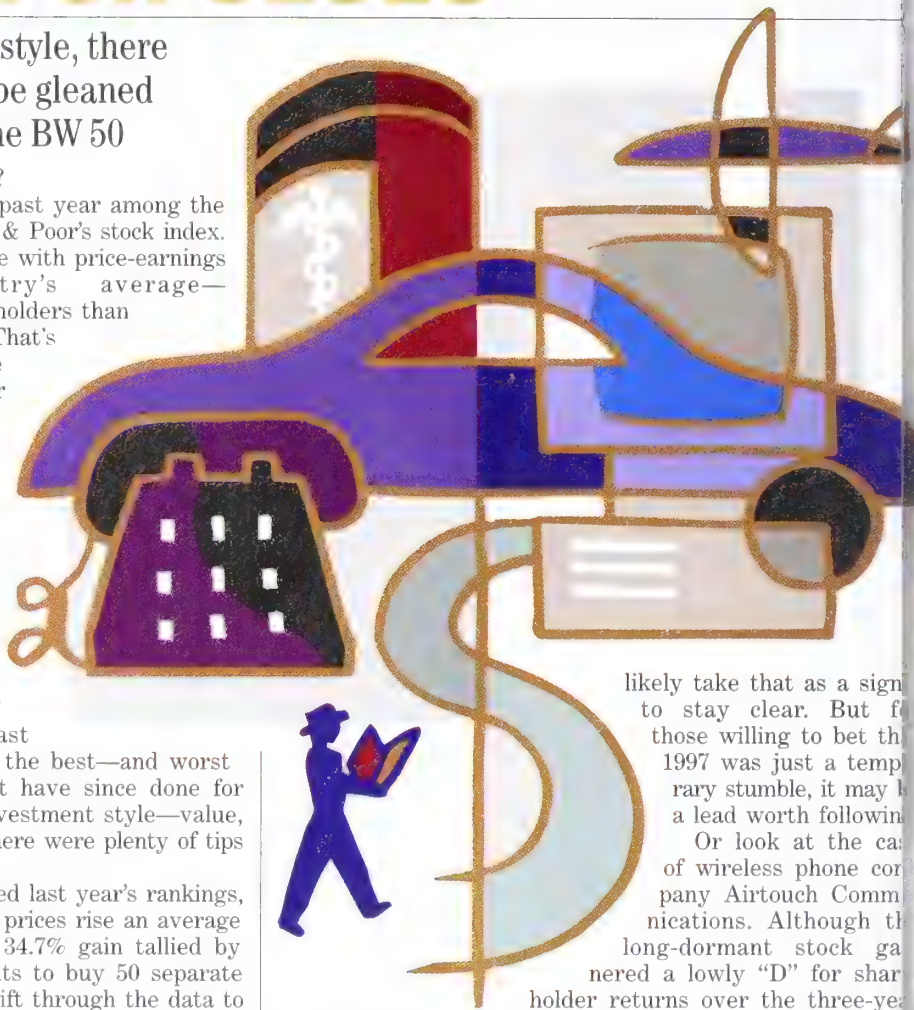
Whatever your investment style, there are lots of valuable tips to be gleaned from the performance of the BW 50

Cheaper stocks do better, right? Wrong. At least not over the past year among the 500 companies in the Standard & Poor's stock index. Cheap stocks—defined as those with price-earnings ratios below their industry's average—actually returned a bit less to shareholders than those priced at premium multiples. That's one surprise we discovered when we went back and checked the first-year investment performance of the companies in BUSINESS WEEK's exclusive rankings of the S&P 500.

The reason for the look back was simple: the BW 50 and the accompanying Performance and Industry Rankings present a detailed portrait of how America's top companies have done over the last three years. But how can active investors use this wealth of data to decide where to put money today? To determine that, we analyzed last year's rankings to see how some of the best—and worst ranked companies on last year's list have since done for shareholders. And whatever your investment style—value, growth, or somewhere in between—there were plenty of tips to be gleaned.

In the 12 months since we published last year's rankings, the BW 50 companies saw their stock prices rise an average of 47.7%. That was well above the 34.7% gain tallied by the S&P index overall. But who wants to buy 50 separate stocks? The trick is to find ways to sift through the data to select a smaller number of companies likely to deliver top returns.

The best place to start is with the Performance Rankings. With a quick glance through each company's letter grades, you can readily see its individual strengths and weaknesses. That can provide plenty of fodder for screening stocks. Take Gillette Co., for instance, which fell from No. 28 to No. 38 this year. The reason: Despite top grades elsewhere, Gillette received poor marks for one-year sales growth and one-year shareholder returns. Both focus on the short term; over three years, Gillette gets "A" grades in both categories. Momentum investors interested only in growth would



likely take that as a sign to stay clear. But for those willing to bet that 1997 was just a temporary stumble, it may be a lead worth following.

Or look at the case of wireless phone company Airtouch Communications. Although the long-dormant stock gained a lowly "D" for shareholder returns over the three-year period, its soaring shares earned an "A" for investors over the last 12 months. A sign of a turnaround at the company, which jumped from No. 206 to No. 55 on this year's list? Maybe. Airtouch merits an "A" in nearly every other category.

For those who want more to go on, and aren't put off by some number-crunching, the next place to turn is the Industry Rankings. These offer a far more detailed portrait of how the S&P 500 companies performed—and, with the right analysis, some telltale signs that may lead to future stock market profits.

What criteria are most important? It depends on your i

Companies with rising profit margins in 1996 had shareholder returns averaging 36.2% in '97



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LAST YEAR'S EXPERIENCE...

We selected S&P 500 companies using various criteria, and came up with these 12-month total returns for each group

SELECTION CRITERION	RETURN*
COMPANIES WHOSE PROFIT MARGINS GREW	36.2%
COMPANIES IN TOP QUINTILE, RETURN ON INVESTED CAPITAL	37.4
COMPANIES WITH BUSINESS WEEK INDUSTRY RANK OF 1 OR 2	40.5
BUSINESS WEEK 50 AVERAGE	44.5*
S&P 500 AVERAGE	31.3

*Minus stocks removed during the year

...SUGGESTS SOME STOCKS TO CONSIDER NOW

In this year's rankings, these companies fit all three of the criteria—wider profit margins, top quintile return on invested capital, and BW industry rank of 1 or 2

COMPANY	PERFORMANCE RANK	COMPANY	PERFORMANCE RANK
APPLIED MATERIALS	13	PFIZER	12
AVERY DENNISON	193	SCHLUMBERGER	18
CAMPBELL SOUP	131	TELLABS	7
DELL COMPUTER	2	TJX	21
GILLETTE	38	UNITED TECHNOLOGIES	151
HERSHEY FOODS	98	US AIRWAYS GROUP	14
INTEL	4	USX-U.S. STEEL GROUP	225
MICROSOFT	1		

DATA: STANDARD & POOR'S COMPUSTAT, A DIVISION OF THE MCGRAW-HILL COMPANIES

vestment philosophy. Value investors looking for underappreciated gems may want to focus on stocks with low price/earnings ratios relative to industry peers. For growth-oriented investors, a winning company may be one that outperforms rivals. Digging into the numbers from last year's Industry Rankings, we discovered three key guides to use when you're ready to sift through this year's data.

RANK WITHIN INDUSTRY COUNTS. Companies that ranked No. 1 or No. 2 in their industry a year ago continued to outperform. For the 12 months ended Feb. 27, they boasted average total returns—stock appreciation plus reinvested dividends—of 40.5%. That's more than nine percentage points above the S&P's overall average on the same basis. And bottom-fishers beware: Companies that ranked near

whose shareholder return fell 26.3%. The group on average performed splendidly, returning 56.8%. That relatively small universe included Dell Computer Corp., which boasted a sterling 298.9% return. Yet even omitting Dell, the other 3 companies returned 38% on average.

Let's say you're building a portfolio today and want to apply those criteria to this year's BW 50 to find stocks that may be worth researching. Who pops up? A total of 15 stocks, which are listed in the second half of the table above. Microsoft Corp. and Dell are there, but so are surprises such as No. 225 USX-U.S. Steel Group.

So do top industry rankings, growing profit margins, and high ROIC provide a passport to stock-market success? Of course not. For one thing, what worked so well in last year's vigorous market might not in a bear market. Also, sorting

Those in the bottom fifth returned 27.6% for investors.

Given the stellar results produced by screening the S&P 500 companies using those three criteria, what kind of performance would an investor get by combining them? It turns out that 14 companies on last year's list were ranked one or two in their industry, had growing profit margins, and were in the top fifth in terms of ROIC. Had you bought their shares, you would probably be very pleased: One of the 14 lost money for investors last year—Andrew Cor

The bottom feeder's picks would include Fruit of the Loom, Polaroid, and Dow Jones

the bottom of their industries underperformed the S&P again last year.

PROFIT MARGINS ARE KEY. One crucial measure of increasing efficiency is improved profit margins. That's why our Industry Rankings include two years of margins. To test how that translates to stock market gains, we did a simple calculation: If you had used last year's rankings to pick stocks with rising profit margins, how would your portfolio have done? Pretty well, indeed. Companies that boasted margin growth in 1996 turned in shareholder returns averaging 36.2% for the 12 months through February. And only 8% of those companies delivered negative returns for shareholders, vs. 13.3% of the overall S&P 500.

STUDY RETURN ON INVESTED CAPITAL. Companies with high return on invested capital often turn in outsize stock market gains. Why? Since ROIC includes profits flowing from all the money a business has working for it, it captures most of any enterprise's ability to deliver total returns to shareholders. That certainly proved true for the companies on our 1997 list: Those ranked in the top one-fifth in terms of ROIC averaged returns of 37.4%.

through the strong performers isn't the only way to pick stocks.

What if you prefer to hunt for bargains near the bottom of the barrel? Say you had taken the opposite approach from that outlined above, and used last year's Industry Rankings to pick laggards with narrowing margins and weak ROIC in the bottom fifth. Turns out you wouldn't have done too poorly either. You would now have a 15-stock portfolio that returned a better-than-average 35.7%, powered by Navistar International Corp.'s 215.6% surge. But leaving Navistar out and the average return sinks to 22.8%—and some of your stocks would be underwater.

Apply those criteria to this year's Industry Rankings, and what companies would you be adding to your portfolio? The bottom feeder's picks would include such stocks as Fruit of the Loom, Polaroid, Novell, and Dow Jones.

The market undoubtedly will give investors new ways to spin the data this year. But as you bring more attention to the market now, applying the lessons of the past year to today's Industry and Performance Rankings may tilt the odds in your favor.

By Robert Bark

THE
BUSINESS
WEEK



BUSINESS WEEK'S PERFORMANCE RANKINGS OF THE S&P 500

What makes a top corporate performer? To determine how the companies in the S&P 500 index stack up against one another, Business Week ranked all 500 using eight key criteria of financial success. We looked at growth in sales, profits, and return to shareholders. To reward consistency, we measured performance over one year and three years. And to get a better fix on which companies squeeze the most out of operations, we analyzed profit margins and return on equity. Using those rankings, we assigned grades for each measure. The top 20% received an A, the next 20% got a B and so on down to the F's in the bottom quintile. Finally, we combined the individual category rankings and added a weighting for sales volume to come up with our overall ranking.

RANK 1997	COMPANY	PERFORMANCE GRADES								INDUSTRY GROUP
		TOTAL RETURN (1 YEAR)	TOTAL RETURN (3 YEARS)	SALES GROWTH (1 YEAR)	SALES GROWTH (3 YEARS)	PROFIT GROWTH (1 YEAR)	PROFIT GROWTH (3 YEARS)	NET MARGIN	RETURN ON EQUITY	
2	MICROSOFT	A	A	A	A	A	A	A	A	Office Equipment & Computers
3	DELL COMPUTER	A	A	A	A	A	A	C	A	Office Equipment & Computers
4	CISCO SYSTEMS	A	A	A	A	B	A	A	A	Office Equipment & Computers
1	INTEL	C	A	A	A	A	A	A	A	Electrical & Electronics
8	COMPAQ COMPUTER	A	A	A	A	A	A	C	B	Office Equipment & Computers
9	MBNA	A	A	A	A	A	A	A	A	Banks
21	TELLABS	A	A	A	A	A	A	A	A	Telecommunications
16	EMC	A	A	A	A	A	A	A	A	Office Equipment & Computers
187	COMPUTER ASSOCIATES INTL.	A	B	B	A	A	A	A	A	Office Equipment & Computers
38	MORGAN STANLEY, DEAN WITTER	A	A	A	A	B	A	B	B	Nonbank Financial
37	SCHERING-PLOUGH	A	A	A	B	B	B	A	A	Health Care
10	PFIZER	A	A	B	B	B	B	A	A	Health Care
77	APPLIED MATERIALS	A	A	B	A	A	A	A	B	Manufacturing
208	US AIRWAYS GROUP	A	A	D	C	A	A	B	A	Transportation
6	MERCK	B	A	A	B	B	B	A	A	Health Care
5	TRAVELERS GROUP	A	A	B	A	C	A	B	B	Nonbank Financial
61	GAP	A	A	A	A	B	B	B	A	Discount & Fashion Retailing
75	SCHLUMBERGER	B	B	A	B	A	A	B	B	Fuel
24	MERRILL LYNCH	B	A	A	A	B	B	C	A	Nonbank Financial
13	SUN MICROSYSTEMS	B	A	A	A	B	A	C	A	Office Equipment & Computers

THE S&P 500

Business Week's Performance Rankings

PERFORMANCE GRADES

INDUSTRY GROUP

			PRICE PER SHARE	TOTAL RETURN (3 YEARS)	SALES GROWTH (3 YEARS)	SALES PER EMPLOYEE (3 YEARS)	EMPHATIC GROWTH (3 YEARS)	PROFIT GROWTH (3 YEARS)	NET MARGIN	RETURN ON EQUITY	
21	55	TJX	A	A	B	A	A	A	D	A	Discount & Fashion Retailing
22	14	BRISTOL-MYERS SQUIBB	A	A	B	C	C	B	A	A	Health Care
23	—	HBO	A	A	A	A	A	A	B	C	Office Equipment & Computers
24	112	CHASE MANHATTAN	C	A	B	A	A	A	A	C	Banks
25	141	CONSECO	D	A	A	A	A	A	B	C	Nonbank Financial
26	40	MGIC INVESTMENT	A	A	B	A	B	A	A	B	Nonbank Financial
27	—	COUNTRYWIDE CREDIT INDUSTRIES	B	A	A	A	A	A	A	B	Nonbank Financial
28	344	GUIDANT	A	A	A	B	A	C	B	A	Health Care
29	357	PACCAR	A	A	A	B	A	C	D	A	Automotive
30	—	OMNICOM GROUP	A	A	A	B	B	B	C	A	Service Industries
31	47	NORTHERN TELECOM	B	A	A	A	A	A	C	C	Telecommunications
32	—	CHARLES SCHWAB	B	A	A	A	B	A	B	A	Nonbank Financial
33	—	PROGRESSIVE	A	A	A	A	B	C	B	B	Nonbank Financial
34	—	SUNAMERICA	B	A	A	B	A	A	A	C	Nonbank Financial
35	—	STATE STREET	B	A	A	A	B	B	A	B	Banks
36	—	LEHMAN BROTHERS HOLDINGS	A	A	A	C	A	A	D	C	Nonbank Financial
37	—	PARAMETRIC TECHNOLOGY	F	A	A	A	A	A	A	A	Office Equipment & Computers
38	28	GILLETTE	C	A	D	A	A	B	A	A	Consumer Products
39	146	CORESTATES FINANCIAL	A	A	D	A	B	A	A	A	Banks
40	22	NORWEST	A	A	C	B	B	B	A	B	Banks
41	42	GENERAL ELECTRIC	B	A	B	B	C	C	B	A	Conglomerates
42	41	FANNIE MAE	A	A	B	B	C	C	B	B	Nonbank Financial
43	119	HALLIBURTON	B	B	A	B	A	A	D	B	Fuel
44	98	HOME DEPOT	A	C	A	A	B	B	D	C	Discount & Fashion Retailing
45	17	FREDDIE MAC	B	A	A	A	C	C	B	B	Nonbank Financial
46	33	HEALTHSOUTH	C	B	A	A	A	A	B	B	Health Care
47	—	CLEAR CHANNEL COMMUNICATIONS	A	A	A	A	A	A	B	F	Publishing & Broadcasting
48	193	RITE AID	B	B	A	A	A	A	F	D	Health Care
49	79	ALLSTATE	B	A	D	D	A	A	A	B	Nonbank Financial
50	12	NATIONSBANK	D	A	A	B	B	B	A	C	Banks
51	—	OWENS-ILLINOIS	A	A	A	C	A	A	C	B	Containers & Packaging
52	105	INTERPUBLIC GROUP	A	B	A	B	B	A	C	A	Service Industries
53	149	DAYTON HUDSON	A	A	B	C	A	B	D	B	Discount & Fashion Retailing
54	—	SUMMIT BANCORPORATION	A	A	C	A	B	A	A	C	Banks
55	206	AIRTOUGH COMMUNICATIONS	A	D	A	A	A	A	A	D	Telecommunications
56	—	NORTHERN TRUST	A	A	B	B	B	B	A	B	Banks
57	106	CATERPILLAR	B	B	B	C	B	B	B	A	Manufacturing
58	182	NORTHROP GRUMMAN	A	A	C	B	A	A	D	C	Aerospace & Defense
59	145	PARKER HANNIFIN	A	B	B	B	A	A	C	B	Manufacturing
60	56	WARNER-LAMBERT	A	A	B	C	C	C	B	A	Health Care



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THE S&P 500

Business Week's Performance Rankings

			PERFORMANCE GRADES							INDUSTRY GROUP	
			1990-91 3 YEARS	1991-92 3 YEARS	1992-93 3 YEARS	1993-94 3 YEARS	PROFIT GROWTH 3 YEARS	NET INCOME	RETURN ON EQUITY		
101	26	U.S. BANCORP	B	A	D	A	F	A	A	C	Banks
102	11	ORACLE	F	D	A	A	C	A	B	A	Office Equipment & Computers
103	121	MARRIOTT INTERNATIONAL	B	B	A	B	C	B	D	B	Leisure Time Industries
104	272	DANA	A	B	B	C	B	B	D	B	Automotive
105	155	PITNEY BOWES	B	A	C	C	C	C	A	A	Office Equipment & Computers
106	99	CLOROX	B	A	B	C	C	C	B	A	Consumer Products
107	62	PROCTER & GAMBLE	B	B	D	D	C	C	B	A	Consumer Products
108	59	NATIONAL CITY	C	B	D	A	C	B	A	B	Banks
109	223	WAL-MART STORES	A	C	B	B	B	C	D	B	Discount & Fashion Retailing
110	101	AUTOMATIC DATA PROCESSING	B	C	B	B	C	C	A	B	Office Equipment & Computers
111	94	PNC BANK	C	B	C	C	C	A	A	B	Banks
112	81	AMERICAN EXPRESS	B	A	C	D	C	C	B	B	Nonbank Financial
113	66	BANK OF NEW YORK	A	A	D	C	C	C	A	B	Banks
114	214	COLUMBIA ENERGY GROUP	C	A	A	A	B	D	C	C	Utilities
115	180	COMERICA	A	A	D	C	B	C	A	B	Banks
116	265	MEREDITH	A	A	C	D	B	A	B	B	Publishing & Broadcasting
117	196	LOWE'S	A	D	A	B	B	B	D	C	Discount & Fashion Retailing
118	245	DRESSER INDUSTRIES	B	B	B	B	B	B	D	B	Manufacturing
119	25	COCA-COLA	D	B	D	D	B	B	A	A	Consumer Products
120	135	HOUSEHOLD INTERNATIONAL	C	A	C	D	B	B	A	C	Nonbank Financial
121	162	XEROX	B	B	D	F	B	B	C	A	Office Equipment & Computers
122	273	MASCO	A	B	B	F	B	A	B	B	Housing & Real Estate
123	191	MBIA	A	B	A	B	B	C	A	D	Nonbank Financial
124	65	TEXACO	D	C	D	B	A	A	C	B	Fuel
125	252	FEDERATED DEPARTMENT STORES	C	C	D	A	A	A	D	D	Discount & Fashion Retailing
126	280	CASE	C	B	B	C	B	A	C	B	Manufacturing
127	184	ECOLAB	B	B	B	C	B	B	B	A	Consumer Products
128	282	THOMAS & BETTS	C	C	C	A	A	A	C	C	Electrical & Electronics
129		ADOBE SYSTEMS	C	F	B	B	B	A	A	A	Office Equipment & Computers
130	232	BIOMET	A	C	C	B	B	B	A	B	Health Care
131	183	CAMPBELL SOUP	C	B	D	D	A	C	B	A	Food
132	288	BELL ATLANTIC	C	C	D	A	D	B	B	B	Telecommunications
133	190	ST. PAUL	C	C	C	C	A	B	A	C	Nonbank Financial
134	115	EMERSON ELECTRIC	C	C	B	B	C	C	B	B	Electrical & Electronics
135	170	MELLON BANK	A	A	F	D	C	B	A	B	Banks
136	355	MAYTAG	A	A	B	F	A	D	C	A	Consumer Products
137	103	FLEET FINANCIAL GROUP	B	A	D	D	B	B	A	B	Banks
138	136	THERMO ELECTRON	D	C	A	A	B	A	C	C	Electrical & Electronics
139	72	PRAXAIR	F	C	C	A	A	B	B	B	Chemicals
140	130	SUNTRUST BANKS	B	A	B	C	C	C	A	C	Banks



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		PERFORMANCE GRADES								INDUSTRY GROUP	
		TOTAL RET. YTD (1 YEAR)	TOTAL RET. YTD (3 YEARS)	TOTAL RET. YTD (5 YEARS)	SALES GROWTH (3 YEARS)	PROFIT GROWTH (1 YEAR)	PROFIT GROWTH (3 YEARS)	NET MARGIN	PERF. ON EQUITY		
141	207	SHARED MEDICAL SYSTEMS	B	B	B	B	B	B	C	B	Office Equipment & Computers
142	178	BANKERS TRUST NEW YORK	C	C	C	C	C	B	B	C	Banks
143	108	INGERSOLL-RAND	B	B	C	B	C	B	C	C	Manufacturing
144	350	MANOR CARE	B	C	A	C	A	B	B	B	Health Care
145	238	CHUBB	B	C	A	D	A	C	B	C	Nonbank Financial
146	295	HILTON HOTELS	D	D	A	A	A	B	D	F	Leisure Time Industries
147	281	NEW YORK TIMES	B	A	C	C	A	D	B	C	Publishing & Broadcasting
148	205	CRANE	B	B	B	C	B	B	C	B	Service Industries
149	226	TEXTRON	B	A	B	D	B	C	D	B	Conglomerates
150	19	GREEN TREE FINANCIAL	F	F	A	A	A	C	A	A	Nonbank Financial
151	134	UNITED TECHNOLOGIES	D	A	D	D	B	B	D	A	Aerospace & Defense
152	—	CINCINNATI FINANCIAL	A	A	C	C	A	C	A	F	Nonbank Financial
153	351	DUKE ENERGY	C	D	A	A	D	B	C	D	Utilities
154	329	WESTERN ATLAS	A	B	B	C	A	A	C	D	Fuel
155	481	NAVISTAR INTERNATIONAL	A	C	A	D	A	D	D	C	Automotive
156	93	BANC ONE	B	B	C	B	D	C	A	C	Banks
157	232	FDX	C	C	B	C	A	B	D	C	Transportation
158	—	EQUIFAX	B	B	B	F	B	C	A	A	Nonbank Financial
159	124	EXXON	C	C	D	C	C	B	C	B	Fuel
160	84	CHEVRON	C	C	F	D	B	A	B	B	Fuel
161	—	CONSOLIDATED STORES	B	A	A	A	F	B	F	D	Discount & Fashion Retailing
162	241	EATON	C	C	C	C	A	C	C	B	Electrical & Electronics
163	219	CONSOLIDATED NATURAL GAS	D	D	A	A	C	A	C	C	Utilities
164	—	HUNTINGTON BANCSHARES	B	B	B	B	D	C	A	C	Banks
165	125	BENEFICIAL	A	A	C	C	D	B	B	C	Nonbank Financial
166	133	HONEYWELL	D	B	B	C	B	B	C	B	Electrical & Electronics
167	73	MCGRAW-HILL	B	B	B	C	F	B	B	B	Publishing & Broadcasting
168	85	REPUBLIC NEW YORK	C	B	B	B	C	C	A	D	Banks
169	393	AETNA	F	D	A	B	A	B	D	D	Nonbank Financial
170	140	MARSH & McLENNAN	B	B	A	A	D	D	C	D	Nonbank Financial
171	91	ATLANTIC RICHFIELD	C	D	F	C	B	A	B	B	Fuel
172	147	UNOCAL	F	D	B	F	A	A	B	A	Fuel
173	137	AIR PRODUCTS & CHEMICALS	D	C	B	C	B	B	B	B	Chemicals
174	95	GTE	D	C	C	D	D	D	B	A	Telecommunications
175	406	SUPERVALU	A	C	D	F	A	A	F	B	Food
176	175	AMR	A	C	D	D	D	A	C	C	Transportation
177	29	LOCKHEED MARTIN	B	B	D	C	D	C	D	A	Aerospace & Defense
178	148	MINNESOTA MINING & MFG.	F	D	C	F	A	B	A	A	Manufacturing
179	89	NEWELL	C	C	B	B	C	C	B	B	Manufacturing
180	321	WORLDCOM	B	A	A	A	C	F	D	F	Telecommunications

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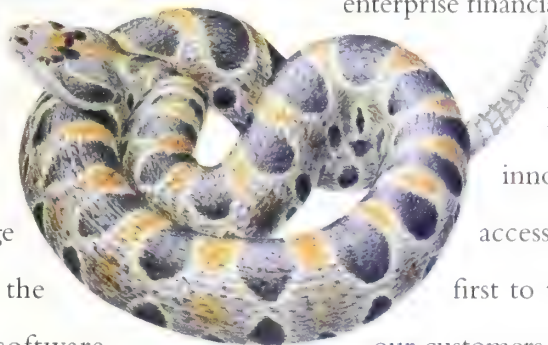


fig. 1



fig. 2

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			PERFORMANCE GRADES							INDUSTRY GROUP	
			TOTAL RETURNS (1 YEAR)	TOTAL RETURNS (3 YEARS)	SALES GROWTH (1 YEAR)	SALES GROWTH (3 YEARS)	PROFIT GROWTH (1 YEAR)	PROFIT GROWTH (3 YEARS)	NET MARGIN		RETURN ON EQUITY
181	316	VIACOM	B	F	C	A	A	A	D	F	Leisure Time Industries
182	—	COGNIZANT	B	INC	C	F	B	A	A	A	Service Industries
183	341	ALLTEL	C	D	D	D	A	B	A	A	Telecommunications
184	225	KEYCORP	C	B	C	D	B	D	A	B	Banks
185	161	U S WEST COMMUNICATIONS GROUP	B	B	D	D	D	D	B	A	Telecommunications
186	250	LIZ CLAIBORNE	C	A	C	D	B	A	C	B	Consumer Products
187	143	SHERWIN-WILLIAMS	D	C	A	B	B	C	C	C	Housing & Real Estate
188	144	ALLIEDSIGNAL	D	B	D	D	B	B	B	A	Conglomerates
189	216	UNITED HEALTHCARE	D	D	B	A	B	B	D	D	Health Care
190	270	GENERAL DYNAMICS	C	C	B	C	B	C	C	B	Aerospace & Defense
191	166	McDONALD'S	C	D	C	C	C	C	A	B	Leisure Time Industries
192	366	H.F. AHMANSON	B	A	F	D	A	D	B	C	Nonbank Financial
193	132	AVERY DENNISON	C	A	D	D	B	B	C	A	Containers & Packaging
194	—	APACHE	F	D	A	A	B	A	A	D	Fuel
195	67	BURLINGTON NORTHERN SANTA FE	D	C	D	A	D	A	B	C	Transportation
196	220	AUTOZONE	D	F	A	A	B	B	C	B	Discount & Fashion Retailing
197	70	RAYCHEM	F	C	C	C	B	A	A	A	Electrical & Electronics
198	263	TORCHMARK	A	B	C	D	C	C	A	B	Nonbank Financial
199	437	HARTFORD FINANCIAL SERVICES GROUP	C	INC	C	D	C	A	B	A	Nonbank Financial
200	203	TIMKEN	C	C	C	C	B	A	C	C	Manufacturing
201	276	CENTEX	A	A	D	D	A	C	D	C	Housing & Real Estate
202	118	CIGNA	C	B	C	F	C	A	C	C	Nonbank Financial
203	138	JOHNSON CONTROLS	C	B	B	B	D	C	F	C	Manufacturing
204	76	WELLS FARGO	F	C	C	A	C	C	A	D	Banks
205	362	UNUM	C	B	F	D	A	A	B	C	Nonbank Financial
206	260	AON	B	B	A	C	C	D	D	D	Nonbank Financial
207	244	KROGER	A	A	C	D	B	B	F	F	Food
208	123	AVON PRODUCTS	D	B	C	D	C	C	C	A	Consumer Products
209	122	J.P. MORGAN	D	C	B	B	D	C	B	D	Banks
210	127	GOLDEN WEST FINANCIAL	C	B	B	B	D	B	A	C	Nonbank Financial
211	—	MERCANTILE BANCORPORATION	B	B	A	A	D	C	B	D	Banks
212	286	GENERAL MOTORS	C	C	C	F	A	D	D	A	Automotive
213	74	PHILIP MORRIS	F	B	D	F	C	C	B	A	Consumer Products
214	63	KIMBERLY-CLARK	F	B	F	B	F	A	C	B	Paper & Forest Products
215	102	SBC COMMUNICATIONS	B	C	C	A	F	D	C	C	Telecommunications
216	159	WACHOVIA	C	B	C	B	D	D	A	C	Banks
217	259	W.W. GRAINGER	D	D	B	C	C	B	C	B	Service Industries
218	128	PIONEER HI-BRED INTERNATIONAL	B	A	D	C	C	C	A	B	Food
219	378	CINCINNATI MILACRON	B	D	B	B	B	B	D	B	Manufacturing
220	254	SIGMA-ALDRICH	C	C	C	C	C	C	A	C	Health Care

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										INDUSTRY GROUP
PERFORMANCE GRADES										
	TOTAL RETURN (1 YEAR)	TOTAL RETURN (3 YEARS)	SALES GROWTH (1 YEAR)	SALES GROWTH (3 YEARS)	PROFIT GROWTH (1 YEAR)	PROFIT GROWTH (3 YEARS)	NET MARGIN	RETURN ON EQUITY		
221 313 ASHLAND	C	C	C	C	A	C	F	D	Fuel	
222 172 UNION CARBIDE	F	D	C	C	B	C	B	A	Chemicals	
223 197 MATTEL	A	B	C	B	D	D	C	C	Leisure Time Industries	
224 189 ALUMINUM CO. OF AMERICA	F	C	D	C	A	C	C	B	Metals & Mining	
225 386 USX-U.S. STEEL GROUP	D	F	D	D	A	B	C	A	Metals & Mining	
226 126 SPRINT	B	A	C	C	D	D	C	D	Telecommunications	
227 49 AMGEN	F	D	C	B	D	A	A	A	Health Care	
228 410 HUMANA	C	F	A	A	A	F	F	D	Health Care	
229 269 KING WORLD PRODUCTIONS	B	D	D	B	C	B	A	B	Leisure Time Industries	
230 258 CORNING	D	D	B	F	B	C	B	A	Manufacturing	
231 251 CINERGY	F	D	A	B	C	B	B	C	Utilities	
232 242 SYSCO	B	D	D	C	C	C	F	A	Food	
233 120 ALLEGHENY TELEDYNE	F	B	F	B	A	D	C	A	Conglomerates	
234 419 TENNECO	D	F	B	A	A	C	D	C	Conglomerates	
235 284 WM. WRIGLEY JR.	C	C	C	C	B	D	A	A	Food	
236 129 GENERAL RE	C	D	F	A	C	C	B	D	Nonbank Financial	
237 — ANADARKO PETROLEUM	D	D	A	B	C	A	A	D	Fuel	
238 303 HARRIS	B	B	C	D	B	B	C	C	Electrical & Electronics	
239 268 TIMES MIRROR	D	A	F	F	B	B	C	A	Publishing & Broadcasting	
240 414 TIME WARNER	A	C	A	A	D	F	F	F	Publishing & Broadcasting	
241 299 SAFECO	C	C	B	C	D	C	B	D	Nonbank Financial	
242 283 B.F. GOODRICH	C	B	A	B	D	B	D	D	Chemicals	
243 311 PEPSICO	D	C	D	F	A	D	C	A	Consumer Products	
244 200 SNAP-ON	D	C	B	C	B	B	B	C	Manufacturing	
245 86 CITICORP	D	A	C	F	D	D	B	C	Banks	
246 399 J.C. PENNEY	B	C	A	C	C	F	F	D	Discount & Fashion Retailing	
247 224 RALSTON PURINA	D	B	D	F	B	B	B	B	Food	
248 194 SEARS, ROEBUCK	F	B	C	C	D	C	D	B	Discount & Fashion Retailing	
249 18 ANDREW	F	D	C	B	C	A	A	B	Electrical & Electronics	
250 361 HOUSTON INDUSTRIES	D	D	A	A	D	D	C	D	Utilities	
251 237 CENDANT	A	B	A	A	F	D	F	F	Service Industries	
252 261 VF	B	C	D	F	B	C	C	B	Consumer Products	
253 229 AT&T	A	C	D	F	D	D	B	B	Telecommunications	
254 447 PG&E	B	D	A	B	D	F	D	D	Utilities	
255 — KLA-TENCOR	D	D	C	A	D	A	B	D	Electrical & Electronics	
256 57 ROYAL DUTCH PETROLEUM	C	C	F	C	D	C	C	C	Fuel	
257 326 AMERICAN GREETINGS	B	D	C	D	B	C	B	C	Leisure Time Industries	
258 31 ORYX ENERGY	C	C	D	D	C	D	A	A	Fuel	
259 285 MAY DEPARTMENT STORES	C	C	C	F	C	D	C	B	Discount & Fashion Retailing	
260 210 BECTON, DICKINSON	C	B	D	D	C	C	B	B	Health Care	

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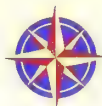
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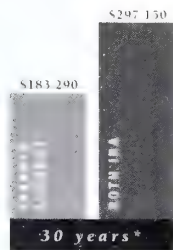
Business Week's Performance Rankings

			PERFORMANCE GRADES							INDUSTRY GROUP	
			TOTAL RETURN (1 YEAR)	SALES GROWTH (1 YEAR)	SALES GROWTH (2 YEARS)	PROFIT GROWTH (1 YEAR)	PROFIT GROWTH (3 YEARS)	NET MARGIN	RETURN ON EQUITY		
261	23	PHILLIPS PETROLEUM	D	D	F	C	D	A	C	B	Fuel
262	164	PPG INDUSTRIES	D	C	D	D	D	C	B	A	Housing & Real Estate
263	296	SOUTHERN	D	D	A	B	D	D	B	D	Utilities
264	377	W.R. GRACE	A	B	F	F	B	F	C	A	Manufacturing
265	249	ALBERTSON'S	C	D	C	D	C	C	D	A	Food
266	131	HARNISCHFEGER INDUSTRIES	F	F	D	A	B	A	D	B	Manufacturing
267	163	USX-MARATHON GROUP	B	B	F	B	F	B	D	C	Fuel
268	305	TRANSAMERICA	C	B	C	F	C	C	B	D	Nonbank Financial
269	247	AEROQUIP-VICKERS	A	B	D	D	D	C	D	B	Manufacturing
270	157	MOBIL	D	C	F	D	C	B	D	C	Fuel
271	352	FLEETWOOD ENTERPRISES	A	B	D	F	B	D	D	B	Housing & Real Estate
272	154	ROHM & HAAS	D	C	F	D	C	B	B	A	Chemicals
273	368	NACCO INDUSTRIES	A	B	F	D	B	C	D	C	Manufacturing
274	398	BLACK & DECKER	A	C	F	F	A	B	D	C	Manufacturing
275	421	NORDSTROM	A	D	C	C	B	D	D	C	Discount & Fashion Retailing
276	309	FPL GROUP	C	C	C	D	C	D	B	D	Utilities
277	360	CONAGRA	D	C	F	F	A	D	D	A	Food
278	327	NUCOR	D	F	B	C	B	C	C	C	Metals & Mining
279	462	KAUFMAN & BROAD HOME	A	C	D	B	D	C	D	C	Housing & Real Estate
280	379	AMP	D	F	D	C	A	D	C	C	Electrical & Electronics
281	334	FIRSTENERGY	B	D	B	D	C	D	B	D	Utilities
282	217	DOW CHEMICAL	D	D	F	F	D	B	B	A	Chemicals
283	318	CVS	A	B	B	B	F	F	F	F	Health Care
284	179	AMERICAN GENERAL	B	C	D	A	D	D	C	D	Nonbank Financial
285	445	GOODYEAR TIRE & RUBBER	C	C	F	F	A	F	D	C	Automotive
286	60	AMOCO	F	D	F	C	D	B	B	C	Fuel
287	314	BROWN-FORMAN	C	C	D	D	C	C	B	A	Consumer Products
288	234	CABLETRON SYSTEMS	F	F	C	A	B	C	A	C	Office Equipment & Computers
289	330	ARMSTRONG WORLD INDUSTRIES	D	C	D	F	C	A	B	A	Consumer Products
290	181	BEMIS	D	D	B	C	C	C	C	C	Containers & Packaging
291	302	COOPER INDUSTRIES	C	D	F	D	B	C	C	C	Electrical & Electronics
292	457	ADOLPH COORS	B	C	D	D	A	C	D	D	Consumer Products
293	100	ANHEUSER-BUSCH	D	C	D	F	C	C	B	A	Consumer Products
294	336	KELLOGG	C	D	D	F	C	D	B	A	Food
295	58	DUPONT	D	B	D	D	F	D	C	B	Chemicals
296	262	NICOR	C	C	C	C	C	C	C	B	Utilities
297	337	NALCO CHEMICAL	D	F	B	F	C	B	B	A	Chemicals
298	325	EDISON INTERNATIONAL	C	C	C	D	D	D	B	D	Utilities
299	356	CONSOLIDATED EDISON	B	C	D	D	C	D	B	D	Utilities
300	275	FREEPORT-McMORAN COPPER & GOLD	F	INC	D	B	C	B	B	B	Metals & Mining

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THE S&P 500

Business Week's Performance Rankings

										INDUSTRY GROUP	
PERFORMANCE GRADES											
		TOTAL RET. 1 YEAR	TOTAL RET. 3 YEARS	SALES GROWTH (1 YEAR)	SALES GROWTH (3 YEARS)	PROFIT GROWTH (1 YEAR)	PROFIT GROWTH (3 YEARS)	NET MARGIN	RETURN ON EQUITY		
301	256	TEXAS UTILITIES	F	D	A	B	D	D	B	D	Utilities
302	317	MONSANTO	A	A	A	F	F	F	D	D	Chemicals
303	426	COMCAST	A	B	A	A	F	F	F	F	Publishing & Broadcasting
304	365	WINN-DIXIE STORES	A	C	D	D	D	F	C	C	Food
305	173	SONAT	F	D	A	A	D	C	D	D	Utilities
306	87	ALBERTO-CULVER	F	C	C	B	C	B	D	C	Consumer Products
307	215	TENET HEALTHCARE	B	B	B	A	F	F	F	F	Health Care
308	107	BESTFOODS	C	B	F	D	D	C	D	B	Food
309	209	GENERAL MILLS	D	D	D	D	D	C	C	A	Food
310	450	H&R BLOCK	A	D	A	F	B	D	B	D	Nonbank Financial
311	27	ELI LILLY	B	A	B	B	F	F	F	F	Health Care
312	69	CHRYSLER	D	C	F	D	D	D	D	A	Automotive
313	264	GENUINE PARTS	D	D	D	C	C	C	C	B	Service Industries
314	340	SAFETY-KLEEN	B	D	C	C	C	C	C	C	Service Industries
315	156	CROWN CORK & SEAL	F	F	D	A	C	A	D	D	Containers & Packaging
316	192	BOEING	D	B	A	A	F	F	F	F	Aerospace & Defense
317	153	BAKER HUGHES	D	C	A	B	F	D	D	F	Fuel
318	88	LOEWS	F	C	F	B	F	A	D	D	Nonbank Financial
319	176	BAXTER INTERNATIONAL	C	C	B	C	F	D	D	D	Health Care
320	298	MICRON TECHNOLOGY	F	F	B	A	C	F	B	D	Electrical & Electronics
321	315	AMERICAN ELECTRIC POWER	D	D	C	D	C	D	B	C	Utilities
322	—	LUCENT TECHNOLOGIES	A	INC	B	B	F	F	F	D	Telecommunications
323	266	UST	C	F	D	D	D	D	A	A	Consumer Products
324	292	RAYTHEON	C	D	B	C	F	D	D	D	Electrical & Electronics
325	382	GPU	C	D	D	D	B	B	B	D	Utilities
326	381	DOMINION RESOURCES	D	F	A	B	D	D	C	F	Utilities
327	413	AMEREN	F	F	F	A	C	C	B	C	Utilities
328	363	DATA GENERAL	D	B	B	C	A	F	D	D	Office Equipment & Computers
329	151	ENRON	D	D	A	A	F	F	F	F	Service Industries
330	435	TOYS 'R' US	F	F	B	C	B	C	D	D	Discount & Fashion Retailing
331	441	DTE ENERGY	C	D	D	F	A	D	B	D	Utilities
332	291	NORFOLK SOUTHERN	D	D	D	F	C	C	A	C	Transportation
333	492	BETHLEHEM STEEL	B	F	F	F	C	A	C	B	Metals & Mining
334	332	BURLINGTON RESOURCES	F	F	F	A	D	A	A	D	Fuel
335	346	ENTERGY	D	D	A	B	F	D	D	F	Utilities
336	359	NATIONAL SERVICE INDUSTRIES	B	B	F	F	C	C	C	B	Electrical & Electronics
337	290	PACIFICORP	D	D	A	A	F	F	D	F	Utilities
338	412	TANDY	A	C	F	D	D	D	D	B	Consumer Products
339	174	ONEOK	C	B	F	B	C	B	D	F	Utilities
340	104	COASTAL	B	B	F	F	D	B	D	D	Fuel

THERE ARE LOTS OF WAYS FOR YOUR BUSINESS TO ENTER THE INTERNET.



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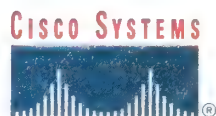
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500										INDUSTRY GROUP	
PERFORMANCE GRADES											
			PRICE PER SHARE	TOTAL RETURN 1 YEAR	SALES GROWTH 1 YEAR	SALES GROWTH (3 YEARS)	PROFIT GROWTH 1 YEAR	PROFIT GROWTH (3 YEARS)	NET MARGIN	RET. ON EQUITY	
341	160	H.J. HEINZ	B	B	F	D	F	D	D	C	Food
342	404	CUMMINS ENGINE	D	F	C	D	A	D	D	C	Manufacturing
343	438	JOSTENS	D	F	D	F	A	D	C	A	Manufacturing
344	306	PERKIN-ELMER	F	B	C	C	C	D	D	C	Electrical & Electronics
345	227	MORTON INTERNATIONAL	D	D	B	F	B	D	B	C	Chemicals
346	423	SUN	B	D	F	B	C	F	F	C	Fuel
347	204	UNION PACIFIC	F	D	A	B	F	D	D	F	Transportation
348	171	BRUNSWICK	D	D	B	C	D	C	D	D	Leisure Time Industries
349	454	WOOLWORTH	D	D	F	F	C	A	D	B	Discount & Fashion Retailing
350	248	TEKTRONIX	B	C	B	B	D	D	D	D	Electrical & Electronics
351	109	MCI COMMUNICATIONS	C	B	C	B	F	F	F	F	Telecommunications
352	233	CSX	D	D	F	D	D	C	C	C	Transportation
353	297	UNION PACIFIC RESOURCES GROUP	F	INC	D	B	C	D	A	B	Fuel
354	—	MIRAGE RESORTS	F	C	D	D	C	B	A	C	Leisure Time Industries
355	324	LIMITED	A	D	C	C	F	F	F	D	Discount & Fashion Retailing
356	415	COOPER TIRE & RUBBER	D	F	B	C	C	D	C	C	Automotive
357	271	CIRCUIT CITY STORES	C	C	C	B	D	D	F	D	Consumer Products
358	395	PENNZOIL	D	D	C	F	A	F	C	C	Fuel
359	338	ALCAN ALUMINUM	F	F	D	F	B	A	C	D	Metals & Mining
360	257	CENTRAL & SOUTH WEST	D	F	D	B	C	D	C	D	Utilities
361	391	ALLERGAN	F	F	F	C	A	D	B	C	Health Care
362	354	CAROLINA POWER & LIGHT	D	C	D	F	D	C	A	C	Utilities
363	—	SEAGRAM	F	F	F	A	D	B	D	F	Consumer Products
364	405	TEXAS INSTRUMENTS	B	A	F	F	D	F	D	F	Electrical & Electronics
365	372	ARCHER DANIELS MIDLAND	C	D	C	D	D	F	D	F	Food
366	417	HARRAH'S ENTERTAINMENT	D	F	D	D	C	A	C	C	Leisure Time Industries
367	213	WENDY'S INTERNATIONAL	F	D	C	B	D	C	C	D	Leisure Time Industries
368	482	INLAND STEEL INDUSTRIES	D	F	B	D	A	D	F	D	Metals & Mining
369	78	FIRST DATA	F	F	C	B	F	D	C	D	Office Equipment & Computers
370	411	PUBLIC SERVICE ENTERPRISE GROUP	C	D	C	F	D	D	B	D	Utilities
371	420	MERCANTILE STORES	B	D	D	D	C	C	D	D	Discount & Fashion Retailing
372	347	MOTOROLA	F	F	C	C	C	D	D	D	Electrical & Electronics
373	456	SCIENTIFIC-ATLANTA	F	F	B	C	A	D	C	D	Telecommunications
374	402	DILLARD'S	D	F	C	D	C	D	D	D	Discount & Fashion Retailing
375	289	ROCKWELL INTERNATIONAL	D	C	C	F	C	D	C	D	Electrical & Electronics
376	422	TELE-COMMUNICATIONS	A	C	B	D	F	F	F	F	Publishing & Broadcasting
377	333	LAIDLAW	D	C	A	B	F	D	F	F	Transportation
378	472	ARMCO	C	F	C	C	A	C	D	F	Metals & Mining
379	202	IKON OFFICE SOLUTIONS	F	F	A	A	F	D	F	F	Conglomerates
380	198	FLUOR	F	F	A	A	F	D	F	D	Service Industries

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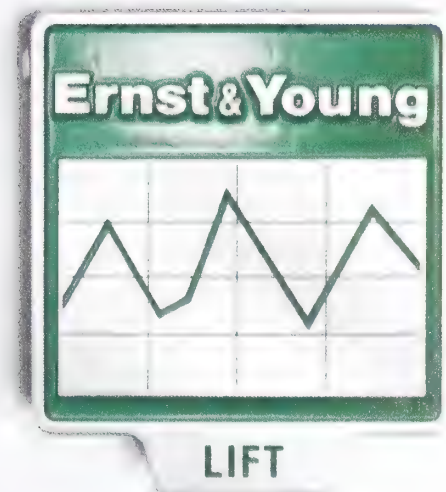
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THE S&P 500

Business Week's Performance Rankings

			PERFORMANCE GRADES							INDUSTRY GROUP	
			TOTAL RET. PN 1 YEAR	TOTAL RETURN 3 YEARS	SALES GROWTH (1 YEAR)	SALES GROWTH (3 YEARS)	PROFIT GROWTH (1 YEAR)	PROFIT GROWTH (3 YEARS)	NET MARGIN	RETURN ON EQUITY	
381	452	CBS	A	C	A	F	F	F	F	F	Publishing & Broadcasting
382	335	ITT INDUSTRIES	C	C	F	D	F	C	F	C	Conglomerates
383	451	BAY NETWORKS	A	D	B	A	F	F	F	F	Office Equipment & Computers
384	278	PEP BOYS-MANNY, MOE & JACK	F	F	B	B	C	C	D	D	Discount & Fashion Retailing
385	240	AMERICAN STORES	D	C	D	F	D	D	F	C	Food
386	440	U S WEST MEDIA GROUP	A	INC	B	A	F	F	F	F	Publishing & Broadcasting
387	158	U.S. SURGICAL	F	D	C	C	D	A	C	D	Health Care
388	396	INTL. FLAVORS & FRAGRANCES	F	F	F	F	B	D	A	B	Chemicals
389	328	PACIFIC ENTERPRISES	C	D	C	F	D	D	C	D	Utilities
390	235	PHELPS DODGE	F	F	D	D	D	C	B	C	Metals & Mining
391	331	PULTE	C	C	C	B	D	D	F	F	Housing & Real Estate
392	342	LONGS DRUG STORES	C	C	D	D	D	C	F	D	Health Care
393	293	KERR-McGEE	D	D	F	D	D	A	B	C	Fuel
394	374	FORT JAMES	B	C	F	C	F	D	F	D	Paper & Forest Products
395	369	BALTIMORE GAS & ELECTRIC	C	D	D	D	D	D	B	D	Utilities
396	287	LSI LOGIC	F	F	D	C	C	C	A	D	Electrical & Electronics
397	487	BALL	C	F	B	F	A	F	F	D	Containers & Packaging
398	397	WORTHINGTON INDUSTRIES	F	F	B	B	D	D	D	C	Metals & Mining
399	367	HERCULES	F	F	F	F	D	D	A	A	Chemicals
400	488	DUN & BRADSTREET	B	C	F	F	D	D	A	F	Nonbank Financial
401	385	PP&L RESOURCES	F	F	D	D	D	C	B	D	Utilities
402	312	ST. JUDE MEDICAL	F	D	B	A	D	F	C	F	Health Care
403	177	GENERAL SIGNAL	F	F	F	C	D	C	C	B	Electrical & Electronics
404	468	NATIONAL SEMICONDUCTOR	F	D	D	D	D	D	B	C	Electrical & Electronics
405	294	PEOPLES ENERGY	D	D	F	D	D	B	C	C	Utilities
406	485	DIGITAL EQUIPMENT	A	D	F	F	C	F	F	D	Office Equipment & Computers
407	408	NEWMONT MINING	F	F	A	A	F	D	D	F	Metals & Mining
408	152	SARA LEE	B	B	D	D	F	F	F	F	Food
409	476	McDERMOTT INTERNATIONAL	A	D	C	D	D	F	F	F	Manufacturing
410	370	GREAT ATLANTIC & PACIFIC TEA	F	D	F	F	D	A	F	D	Food
411	319	ECHLIN	B	D	B	B	F	F	F	F	Automotive
412	343	HASBRO	C	C	C	D	F	D	D	D	Leisure Time Industries
413	425	UNION CAMP	C	F	B	C	D	F	F	F	Paper & Forest Products
414	388	NORTHERN STATES POWER	C	D	D	D	D	D	B	D	Utilities
415	400	MEAD	D	F	C	F	D	C	D	F	Paper & Forest Products
416	376	EASTERN ENTERPRISES	B	C	F	F	D	C	C	D	Utilities
417	444	BROWNING-FERRIS INDUSTRIES	D	F	F	D	D	D	D	C	Service Industries
418	371	ASARCO	F	F	F	C	C	B	D	D	Metals & Mining
419	475	UNISYS	A	C	D	D	F	F	F	F	Office Equipment & Computers
420	433	RYDER SYSTEM	D	D	F	F	D	D	D	C	Transportation



THE S&P 500

Business Week's Performance Rankings

PERFORMANCE GRADES

INDUSTRY GROUP

			TOTAL RETURN (1 YEAR)	TOTAL RETURN (3 YEARS)	SALES GROWTH (1 YEAR)	SALES GROWTH (3 YEARS)	PROFIT GROWTH (1 YEAR)	PROFIT GROWTH (3 YEARS)	NET MARGIN	RETURN ON EQUITY	
421	339	EASTMAN CHEMICAL	C	F	F	F	D	D	C	C	Chemicals
422	424	PECO ENERGY	F	F	C	D	F	D	C	D	Utilities
423	310	REEBOK INTERNATIONAL	F	F	D	D	D	F	D	A	Consumer Products
424	443	AUTODESK	B	F	A	C	F	F	F	F	Office Equipment & Computers
425	427	NIAGARA MOHAWK POWER	D	F	F	F	A	D	C	F	Utilities
426	429	SILICON GRAPHICS	F	F	B	A	D	F	F	F	Office Equipment & Computers
427	387	C.R. BARD	C	D	D	D	D	D	C	C	Health Care
428	416	REYNOLDS METALS	F	F	F	D	A	D	F	F	Metals & Mining
429	211	ENGELHARD	F	F	B	B	F	F	F	D	Metals & Mining
430	389	TRW	D	C	B	D	F	F	F	F	Conglomerates
431	403	RUBBERMAID	C	F	D	D	D	D	C	C	Manufacturing
432	345	LINCOLN NATIONAL	B	B	D	F	F	F	F	F	Nonbank Financial
433	463	R.R. DONNELLEY	C	F	F	F	D	D	D	D	Service Industries
434	484	DSC COMMUNICATIONS	F	F	B	B	D	F	D	F	Telecommunications
435	428	KMART	D	F	D	F	C	F	F	F	Discount & Fashion Retailing
436	430	BRIGGS & STRATTON	F	D	C	F	F	F	D	B	Manufacturing
437	165	ALZA	C	D	B	A	F	F	F	F	Health Care
438	474	BAUSCH & LOMB	D	D	F	F	F	A	D	F	Health Care
439	469	OWENS CORNING	F	F	B	C	D	F	F	F	Housing & Real Estate
440	279	HARCOURT GENERAL	D	D	B	C	F	F	F	F	Conglomerates
441	320	UNICOM	A	D	D	D	F	F	F	F	Utilities
442	243	USF&G	D	D	F	F	D	D	C	D	Nonbank Financial
443	384	SPRINGS INDUSTRIES	C	D	F	F	D	D	D	D	Manufacturing
444	442	EG&G	C	C	D	D	F	F	F	D	Service Industries
445	432	WEYERHAEUSER	D	F	F	F	D	F	D	D	Paper & Forest Products
446	364	INTERNATIONAL PAPER	D	F	F	C	F	F	F	F	Paper & Forest Products
447	300	PHARMACIA & UPJOHN	D	C	F	F	F	F	D	F	Health Care
448	465	CYPRUS AMAX MINERALS	F	F	A	D	D	F	F	F	Metals & Mining
449	167	FRONTIER	C	F	F	B	F	F	F	F	Telecommunications
450	392	WESTVACO	D	F	F	F	D	D	C	D	Paper & Forest Products
451	449	WHIRLPOOL	C	F	D	F	F	F	F	F	Consumer Products
452	186	SEAGATE TECHNOLOGY	F	C	F	B	F	F	F	F	Office Equipment & Computers
453	349	MILLIPORE	F	D	A	B	F	F	F	F	Electrical & Electronics
454	380	GIANT FOOD	D	D	D	D	F	F	F	F	Food
455	467	BOISE CASCADE	F	F	C	C	F	F	F	F	Paper & Forest Products
456	92	CERIDIAN	D	D	B	F	F	F	D	F	Office Equipment & Computers
457	50	COLUMBIA/HCA HEALTHCARE	F	F	F	C	F	F	F	F	Health Care
458	373	TEMPLE-INLAND	D	F	D	C	F	F	F	F	Containers & Packaging
459	308	STANLEY WORKS	C	B	F	F	F	F	F	F	Manufacturing
460	274	PALL	F	F	F	B	F	D	C	D	Conglomerates

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THE S&P 500

Business Week's Performance Rankings

			PERFORMANCE GRADES							INDUSTRY GROUP
			TOTAL RET. 5 YEARS	SALES GROWTH 1 YEAR	PROFIT GROWTH 1 YEAR	PROFIT GROWTH 5 YEARS	NET MARGIN	RETURN ON EQUITY		
461	236	AMERADA HESS	D	F	F	C	F	F	F	Fuel
462	—	TUPPERWARE	F	INC	F	F	F	C	A	Manufacturing
463	436	QUAKER OATS	B	C	F	F	F	F	F	Food
464	375	FORTUNE BRANDS	D	D	D	F	F	F	F	Manufacturing
465	358	DOW JONES	C	D	D	C	F	F	F	Publishing & Broadcasting
466	185	OCCIDENTAL PETROLEUM	F	D	F	F	F	D	F	Fuel
467	390	WILLAMETTE INDUSTRIES	D	D	F	D	F	F	F	Paper & Forest Products
468	277	FOSTER WHEELER	F	F	F	A	F	F	F	Service Industries
469	458	DARDEN RESTAURANTS	A	INC	F	F	F	F	F	Leisure Time Industries
470	460	GEORGIA-PACIFIC GROUP	D	F	F	F	F	F	F	Paper & Forest Products
471	150	EASTMAN KODAK	F	D	F	D	F	F	F	Leisure Time Industries
472	212	FMC	F	F	C	F	F	F	F	Manufacturing
473	464	DELUXE	D	D	F	D	F	F	D	Office Equipment & Computers
474	448	ADVANCED MICRO DEVICES	F	F	A	F	F	F	F	Electrical & Electronics
475	231	RUSSELL	F	F	F	D	F	D	D	Consumer Products
476	255	MALLINCKRODT	F	F	B	F	F	F	F	Health Care
477	431	MOORE	F	F	D	F	F	F	F	Office Equipment & Computers
478	453	POTLATCH	F	F	D	F	F	F	F	Paper & Forest Products
479	489	APPLE COMPUTER	B	F	F	F	F	F	F	Office Equipment & Computers
480	418	CHAMPION INTERNATIONAL	D	F	F	F	F	F	F	Paper & Forest Products
481	455	JOHN H. HARLAND	F	F	F	D	D	F	D	Office Equipment & Computers
482	434	GREAT LAKES CHEMICAL	F	F	F	F	F	C	F	Chemicals
483	409	WASTE MANAGEMENT	F	F	F	F	F	F	F	Service Industries
484	—	TRICON GLOBAL RESTAURANTS	F	INC	F	F	F	F	F	Leisure Time Industries
485	477	PLACER DOME	F	F	D	C	F	F	F	Metals & Mining
486	491	CHARMING SHOPPES	F	F	F	F	D	F	F	Discount & Fashion Retailing
487	471	POLAROID	D	D	F	F	F	F	F	Leisure Time Industries
488	394	BARRICK GOLD	F	F	F	C	F	F	F	Metals & Mining
489	478	BATTLE MOUNTAIN GOLD	F	F	F	B	F	F	F	Metals & Mining
490	348	INCO	F	F	F	F	F	D	F	Metals & Mining
491	446	GENERAL INSTRUMENT	D	F	F	F	F	F	F	Electrical & Electronics
492	493	LOUISIANA-PACIFIC	F	F	F	F	F	F	F	Paper & Forest Products
493	490	STONE CONTAINER	F	F	F	F	F	F	F	Containers & Packaging
494	322	FRUIT OF THE LOOM	F	D	F	F	F	F	F	Consumer Products
495	470	NOVELL	F	F	F	F	F	F	F	Office Equipment & Computers
496	480	HOMESTAKE MINING	F	F	F	F	F	F	F	Metals & Mining
INC	—	PROVIDIAN FINANCIAL	A	INC	A	INC	B	INC	A	Banks
INC	43	TYCO INTERNATIONAL	A	A	INC	INC	INC	INC	INC	Manufacturing
INC	34	3COM	F	F	INC	INC	INC	INC	D	Office Equipment & Computers
INC	—	UNILEVER NV	C	B	INC	INC	INC	INC	INC	Food

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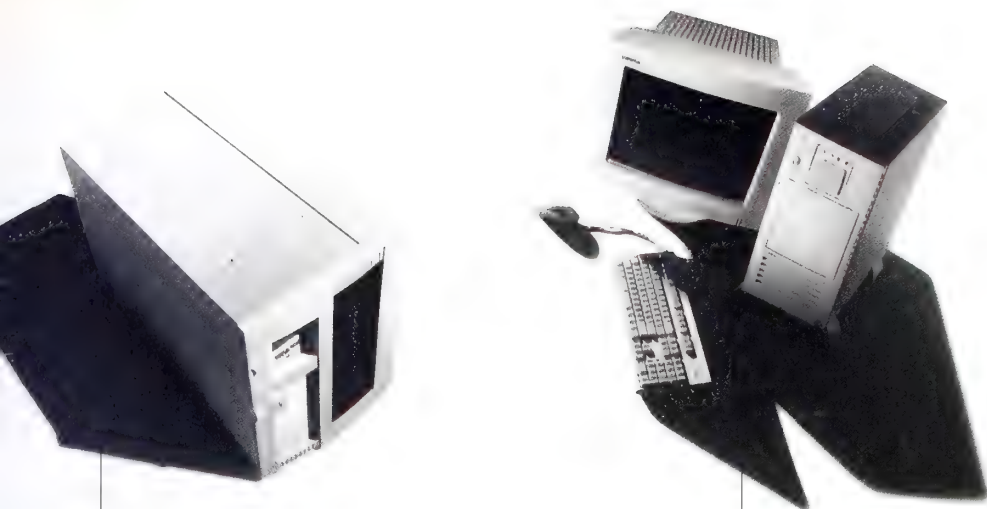
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BUSINESS WEEK'S INDUSTRY RANKINGS OF THE S&P 500

The S&P 500 represents a huge universe, accounting for some 70% of the market capitalization of all U.S. stocks. To find out how each of the companies in the index measures up against its peers, we ranked them within industry groups, using the same factors that go into the overall report card grades. The numbers to derive those grades are shown in these tables, along with a wealth of additional financial information. Each company's rank within its industry is listed to the left of its name, followed by its overall rank. Taken together, they form a vivid picture of how well each company harnesses its resources, given the unique constraints of its industry.

NECESSARY & FOOTNOTES

Companies on this list are from the Standard & Poor's 500. Each company is ranked by the following criteria: one-year total return; three-year average annual sales growth; one-year profit margin; three-year average annual profit margin; net profit margins; and return on equity, with additional weight given to a company's sales. A company's composite rank is calculated using the sum of all of its ranks.

MARKET VALUE

Market price on Feb. 27, 1998, multiplied by the latest available common shares outstanding.

ONE-YEAR TOTAL RETURN

Annual dividend per share, reinvested, plus price on Feb. 27, 1998, price per share, as a percentage of Feb. 27, 1997, price per share.

THREE-YEAR TOTAL RETURN

Annual dividend per share, reinvested, plus price on Feb. 27, 1998, price per share, as a percentage of Feb. 28, 1995, price per share.

SALES

Latest available sales through the most recent 12 months ending Jan. 31, 1998. Includes all sales and other operating revenues. For banks, this includes all banking operations revenues.

THREE-YEAR SALES GROWTH

Calculated using the least squares method. Data for 1997 and 1996 are as reported by company in 1997.

PROFITS

Latest available profits through the most recent 12 months ending Jan. 31, 1998. Net income from continuing operations before extraordinary items.

THREE-YEAR PROFITS GROWTH

Calculated using the least squares method. Data for 1997 and 1996 are as reported by company in 1997. If results for the earliest year are negative, the average is for two years.

NET MARGINS

Net income from continuing operations before extraordinary items as a percent of sales.

RETURN ON INVESTED CAPITAL

Net income available for shareholders as a percent of debt and equity funds.

RETURN ON EQUITY

Net income available for shareholders divided by total equity.

RECENT SHARE PRICE

Price for a single share of a company's most widely traded issue of common stock as of the close of trading Feb. 27, 1998.

HIGH/LOW PRICE

Trading range for the company's common stock, Feb. 27, 1997, to Feb. 27, 1998.

P-E RATIO

Price-earnings ratio based on latest 12 months' earnings and Feb. 27, 1998, stock price.

DIVIDEND YIELD

Annual dividend rate as a percent of the Feb. 27 stock price.

EARNINGS PER SHARE

Primary earnings per share, excluding extraordinary profit or loss, divided by number of common and common equivalent shares.

EARNINGS PER SHARE ESTIMATES

Analysts' consensus estimates for 1998 compiled as of Feb. 19 by I/B/E/S International Inc., New York, N.Y. I/B/E/S is a registered trademark of I/B/E/S International Inc.

(a) Data as of September, 1997.

(b) Data as of October, 1997.

(c) Total return from June 11, 1997.

(d) Total return from Sept. 17, 1997.

(e) Two-year growth rate.

(x) Sales include excise taxes.

(y) Sales include other income.

(z) Sales include excise taxes and other income.

NA=not available. NM=not meaningful.

NC=not calculable. INC=Incomplete.

† Because BUSINESS WEEK is owned by McGraw-Hill, the S&P 500 Scoreboard does not include a forecast of the company's earnings.

Note: Data compiled by Standard & Poor's Compustat, a division of The McGraw-Hill Companies, from sources such as statistical services, registration statements, and company reports that SPC believes to be reliable but are not guaranteed by SPC or BUSINESS WEEK as to correctness or completeness. This material is not an offer to buy or sell any security.

Additional data: I/B/E/S International Inc., New York, N.Y. I/B/E/S is a registered trademark of I/B/E/S International Inc.

THE S&P 500

Business Week's Industry Rankings

MARKET VALUE

SALES

PROFITABILITY

FEB. 27,
1998
\$ MIL.

TOTAL
RETURN
1 YEAR

TOTAL
RETURN
(3 YEARS)

12
MONTHS
1997
\$ MIL.

CHANGE
FROM
1996
%

3 YEAR
AVERAGE
CHANGE
%

12
MONTHS
1997
\$ MIL.

CHANGE
FROM
1996
%

1 AEROSPACE & DEFENSE

INDUSTRY AVERAGE			22134.1	38.7	165.1	22359.4	14	13.7	583.4	-37
1	58	NORTHROP GRUMMAN	9279.1	97.1	236.0	9153.0	6	12.3	407.0	54
2	151	UNITED TECHNOLOGIES	20459.0	20.2	186.0	24713.0y	5	5.1	1072.0	18
3	177	LOCKHEED MARTIN	22637.5	36.2	160.1	28069.0	4	8.0	1300.0	-3
4	190	GENERAL DYNAMICS	5484.8	32.1	98.8	4062.0	13	10.6	316.0	17
5	316	BOEING	52810.1	7.8	144.8	45800.0	29	32.4	-178.0	NM

2 AUTOMOTIVE

INDUSTRY AVERAGE			18964.7	70.2	108.4	45208.9	5	7.1	1993.2	28
1	29	PACCAR	4925.8	109.4	242.1	6751.9	47	12.4	344.6	71
2	100	FORD MOTOR	67988.7	79.1	147.0	153627.0	5	6.3	6920.0	56
3	104	DANA	5730.3	80.7	142.4	8770.3y	11	8.3	369.1	21
4	155	NAVISTAR INTERNATIONAL	2199.2	215.6	109.5	6753.0	21	4.6	173.0	198
5	212	GENERAL MOTORS	48792.5	30.5	86.5	153781.0y	6	-0.5	6698.0	35
6	285	GOODYEAR TIRE & RUBBER	10829.7	32.0	100.3	13155.1	0	2.0	558.7	449
7	312	CHRYSLER	25206.5	19.0	104.7	58622.0	-1	6.0	2805.0	-25
8	356	COOPER TIRE & RUBBER	1816.1	15.7	-14.3	1813.0	12	8.9	122.4	13
9	411	ECHLIN	3193.1	49.3	57.4	3607.1	10	15.6	-52.5	NM

3 BANKS

INDUSTRY AVERAGE			20559.9	43.2	213.9	7532.6	9	17.0	1091.6	10
1	6	MBNA	17949.0	66.9	385.2	4215.8a	41	35.0	583.6a	34
2	24	CHASE MANHATTAN	52230.5	25.9	238.1	27365.0	10	30.6	3708.0	51
3	35	STATE STREET	9941.8	52.6	303.9	3007.0y	22	19.5	380.3	29
4	39	CORESTATES FINANCIAL	16868.9	64.9	213.6	3999.7a	2	21.4	792.2a	23
5	40	NORWEST	31102.6	65.9	242.0	9223.1	8	15.4	1351.0	17
6	50	NATIONSBANK	48784.9	14.4	199.3	20368.0	23	16.6	3077.0	30
7	54	SUMMIT BANCORPORATION	8774.4	61.0	190.7	2280.0	9	28.3	371.0	31
8	56	NORTHERN TRUST	8484.8	81.6	375.2	2022.0y	16	15.1	309.4	20
9	63	FIRST CHICAGO NBD	23763.6	40.1	190.6	9594.0y	-1	35.9	1525.0	6
10	70	SYNOVUS FINANCIAL	6168.2	53.3	324.2	1162.8	11	16.1	165.2	18
11	71	BB&T	8335.6	61.9	204.1	2257.6y	13	17.3	359.9	9
12	73	BANKBOSTON	14497.8	35.9	260.3	5942.0y	6	9.2	879.2	35
13	79	FIFTH THIRD BANCORP	12262.8	42.1	265.4	1917.5	10	17.7	401.2	20
14	82	FIRST UNION	33490.2	21.4	160.5	11787.0y	5	27.8	1896.0	17
15	94	BANKAMERICA	53324.4	36.4	248.8	21318.0	6	11.0	3210.0	12
16	101	U.S. BANCORP	28379.6	44.9	220.5	6456.6	5	38.4	838.5	-31
17	108	NATIONAL CITY	13774.1	31.9	163.1	4200.9y	4	19.7	807.4	10
18	111	PNC BANK	16673.9	33.8	147.4	6522.7y	6	10.0	1052.5	6
19	113	BANK OF NEW YORK	21954.7	53.9	281.1	5124.0y	2	7.1	1104.0	8
	115	COMERICA	10539.4	67.2	293.1	2935.8y	3	7.0	530.5	27
21	135	MELLON BANK	15814.2	56.0	265.7	3268.0y	1	6.4	771.0	5
22	7	FLEET FINANCIAL GROUP	19693.2	36.2	183.2	6472.0	1	6.5	1303.0	14
23	14	SUNTRUST BANKS	15480.8	43.4	191.0	4508.2	13	11.7	667.3	8

RANK 1996	RETURN ON INVESTED CAPITAL	RETURN ON COMMON EQUITY	INVESTMENT DATA					
			RECENT SHARE PRICE \$	12-MONTH HIGH/LOW \$	P-E RATIO	DIVIDEND YIELD	EARNINGS PER SHARE 1997	ESTIMATED EARNINGS PER SHARE 1998
7	9.3	10.5	97	100/65	23	1.36	4.22	5.20
1	7.6	16.3	139	139/72	23	1.15	5.98	6.98
9	16.7	23.0	89	91/67	21	1.39	4.21	4.81
0	7.3	24.1	117	117/78	19	1.37	6.09	6.48
5	15.8	17.0	87	92/63	17	1.88	4.99	5.45
1	-0.9	-1.4	54	61/43	-301	1.03	-0.18	2.30
6	7.6	23.9	51	53/31	14	2.26	3.60	4.38
4	8.8	22.9	63	67/32	14	0.95	4.41	4.58
0	3.5	23.1	57	59/30	10	2.97	5.62	5.31
9	9.3	21.7	55	57/31	16	1.98	3.49	3.84
0	6.8	14.8	30	32/9	15	NA	1.96	2.49
4	5.7	27.9	69	72/52	8	2.90	8.62	8.91
8	11.8	15.8	69	71/49	20	1.73	3.53	5.22
3	13.8	24.7	39	40/28	10	4.12	4.09	5.01
7	11.8	14.7	23	28/18	15	1.65	1.55	1.78
5	-3.2	-5.6	51	53/30	-61	1.78	-0.83	2.29
3	8.7	15.8	82	85/53	21	1.96	3.88	4.75
6	8.2	30.2	36	38/18	31	1.01	1.15	1.51
9	9.4	16.2	124	127/85	15	2.00	8.03	9.63
9	13.7	19.1	62	64/33	27	0.78	2.32	2.70
5	11.5	25.4	84	85/47	21	2.37	3.96	4.24
5	6.7	19.0	41	42/22	23	1.61	1.75	2.03
4	6.1	14.4	69	72/54	16	2.22	4.17	4.83
5	10.5	14.7	50	54/29	24	2.17	2.09	2.68
8	9.4	17.5	76	77/36	29	1.10	2.66	3.02
8	8.3	18.9	82	86/51	17	2.14	4.90	5.40
4	16.0	19.1	35	35/20	38	1.02	0.93	1.11
5	7.1	17.3	62	65/35	24	2.00	2.60	3.49
6	10.2	18.4	100	101/62	18	2.33	5.65	6.50
2	14.7	17.6	79	84/46	31	1.11	2.54	3.02
5	9.0	15.8	53	53/38	18	2.81	2.99	3.83
3	8.7	15.7	78	82/50	18	1.78	4.32	4.86
8	4.9	14.1	115	118/70	34	1.83	3.34	6.16
2	9.3	18.9	65	68/45	18	2.82	3.66	4.08
1	6.5	19.2	56	59/37	17	2.81	3.28	3.66
3	14.0	21.9	59	59/33	22	1.78	2.71	3.07
7	5.1	18.6	101	101/54	32	1.27	3.19	5.49
6	10.1	19.5	62	66/36	22	2.12	2.88	3.21
9	10.6	17.2	79	81/55	17	2.49	4.74	5.17
4	8.0	12.8	74	75/44	24	1.36	3.13	3.48



Credit King

For the second year in a row, credit-card champ MBNA tops the banking group, moving up to No. 6 in the BW 50. One of the biggest card lenders in the country, MBNA continues to cash in on a formula of careful credit checks and marketing through affinity groups. And thanks to cost-cutting and consolidation, the industry had a strong showing overall. But beware: Looming pitfalls for most card players this year include problem loans in Asia, high takeover premiums, and a slowdown in loan demand.

FOOTNOTES TO TABLES APPEAR ON PAGE 123;
ALPHABETICAL INDEX OF COMPANIES
BEGINS ON PAGE 150

THE S&P 500 Business Week's Industry Rankings

			MARKET VALUE			SALES			PROFITABILITY	
			FEB. 27 1998 \$ MIL.	TOTAL RETURN (1 YEAR)	TOTAL RETURN (3 YEARS)	12 MONTHS 1997 \$ MIL.	CHANGE FROM 1996 %	3 YEAR AVERAGE CHANGE %	12 MONTHS 1997 \$ MIL.	CHANGE FROM 1996 %
24	142	BANKERS TRUST NEW YORK	11465.2	32.8	119.2	8843.0y	8	10.9	866.0	13
25	156	BANC ONE	36413.6	41.3	160.2	10401.1	8	14.2	1305.7	-22
26	164	HUNTINGTON BANCSHARES	6878.5	38.4	171.2	2246.2y	17	16.7	292.7	-4
27	168	REPUBLIC NEW YORK	6576.8	29.8	159.1	3209.9	13	14.1	449.1	7
28	184	KEYCORP	15346.0	32.0	169.8	6011.0	6	4.0	919.0	17
29	204	WELLS FARGO	27741.3	5.7	113.4	9161.0	8	27.2	1155.0	8
30	209	J.P. MORGAN	21070.0	15.3	107.5	12353.0y	15	13.2	1465.0	-7
31	211	MERCANTILE BANCORPORATION	7247.3	46.0	147.6	2170.6	20	22.5	204.6	-17
32	216	WACHOVIA	12543.0	31.1	150.9	4247.0y	8	12.6	592.8	-22
33	245	CITICORP	60062.4	12.8	212.1	30300.0y	5	1.6	3591.0	-5
INC	INC	PROVIDIAN FINANCIAL	5404.4	92.9c	NA	1217.1y	21	NA	191.5	20

4 CHEMICALS

INDUSTRY AVERAGE			12666.7	14.5	78.4	7800.5	4	1.9	564.7	-13
1	139	PRAXAIR	7538.1	2.1	117.7	4735.0	6	22.4	416.0	48
2	173	AIR PRODUCTS & CHEMICALS	9878.2	12.1	79.6	4751.7	14	9.7	489.9	15
3	222	UNION CARBIDE	5722.0	-0.1	71.7	6502.0	6	9.5	676.0	14
4	242	B.F. GOODRICH	2682.8	26.8	143.6	3373.0	19	17.5	113.2	-2
5	272	ROHM & HAAS	6262.5	14.1	95.3	3999.0	0	4.0	410.0	13
6	282	DOW CHEMICAL	20748.2	16.7	53.1	20018.0y	0	-0.1	1808.0	-5
7	295	DUPONT	69373.2	15.9	136.6	45079.0z	3	4.6	2405.0	-34
8	297	NALCO CHEMICAL	2680.4	11.7	27.5	1433.7	10	2.6	163.4	12
9	302	MONSANTO	30316.5	55.2	276.2	7514.0	18	-6.1	294.0	-29
10	345	MORTON INTERNATIONAL	4308.1	11.7	62.3	2519.6y	13	-10.5	230.3	26
11	388	INTL. FLAVORS & FRAGRANCES	5025.0	2.2	4.1	1426.8	-1	2.4	218.2	15
12	399	HERCULES	4766.8	5.7	16.1	1866.0	-9	-13.0	324.0	0
13	421	EASTMAN CHEMICAL	5122.6	23.8	30.2	4678.0	-2	1.8	286.0	-25
14	482	GREAT LAKES CHEMICAL	2909.6	5.4	-16.5	1311.2	-3	-17.5	71.8	-40

5 CONGLOMERATES

INDUSTRY AVERAGE			32395.5	17.2	94.6	15667.7	12	11.6	1069.2	6
1	41	GENERAL ELECTRIC	254454.5	50.4	203.4	90840.0y	15	15.2	8203.0	13
2	149	TEXTRON	12353.7	51.8	191.3	10544.0y	14	3.6	558.0	16
3	188	ALLIEDSIGNAL	23764.7	19.9	135.5	14472.0	4	3.4	1170.0	15
4	233	ALLEGHENY TELEDYNE	4746.0	6.8	150.0	3745.1	-2	13.7	297.6	31
5	234	TENNECO	7001.3	8.0	15.6	7220.0	10	20.7	361.0	66
6	379	IKON OFFICE SOLUTIONS	4386.3	-22.5	21.2	5362.3	24	27.2e	114.7	-34
7	382	ITT INDUSTRIES	4056.7	35.9	85.5	8777.1	1	3.6	113.7	-50
8	430	TRW	6758.4	8.5	80.0	10831.3	10	5.7	-48.5	NM
9	440	HARCOURT GENERAL	3820.8	17.3	52.3	3823.6y	14	9.8	-144.2	NM
10	460	PALL	2612.4	-4.5	11.0	1061.8	-2	12.8	67.0	-51

			INVESTMENT DATA					
NET MARGIN 1996	RET. IRON ON INVESTED CAP. TAL.	RETURN ON COMMON EQUITY	RECENT SHARE PRICE \$	12-MONTH HIGH/LOW \$	P-E RATIO	DIVIDEND YIELD	EARNINGS PER SHARE 1997	ESTIMATED EARNINGS PER SHARE 1998
9.3	3.8	14.3	118	134/74	15	3.38	7.66	9.04
7.3	6.0	12.8	57	58/36	28	2.45	1.99	3.59
5.8	6.5	15.0	36	39/23	24	2.23	1.52	2.00
4.8	5.2	11.9	121	122/83	15	1.65	7.88	8.49
3.8	6.9	17.7	35	37/24	17	2.68	2.07	2.32
2.6	6.0	8.8	322	350/245	25	1.62	12.64	15.34
4.7	4.0	12.5	120	126/93	17	3.18	7.17	8.11
3.5	5.8	8.7	56	62/35	34	2.23	1.65	3.04
9.3	6.6	16.1	80	84/54	27	2.21	2.94	4.46
3.1	8.4	16.3	132	145/102	18	1.74	7.33	9.42
5.9	19.3	32.0	57	58/29	28	0.35	2.00	2.51
8.7	12.8	19.1	58	64/46	19	2.01	3.10	3.57
5.3	7.4	18.9	48	58/39	19	1.05	2.53	2.71
0.2	10.1	18.9	84	90/66	19	1.43	4.43	4.38
9.7	16.9	27.4	46	57/40	10	1.94	4.53	3.78
4.1	6.6	9.4	50	50/35	32	2.22	1.53	3.01
9.1	17.3	22.6	102	104/71	16	1.96	6.39	6.65
9.5	14.2	23.3	92	103/78	12	3.80	7.70	6.40
8.3	13.3	20.5	61	70/50	29	2.06	2.08	3.78
1.2	16.5	22.6	40	42/34	19	2.48	2.10	2.54
6.5	4.8	7.2	51	53/36	107	0.24	0.48	1.34
8.2	12.8	14.6	33	44/30	20	1.45	1.65	1.81
3.2	21.0	21.1	46	53/40	23	3.22	1.99	2.25
5.8	25.9	41.0	48	55/38	15	2.24	3.18	3.37
7.9	8.2	16.3	66	67/51	18	2.69	3.63	3.96
8.9	3.6	4.9	49	55/40	41	1.32	1.19	3.95
7.2	7.4	21.1	46	51/34	41	1.86	1.12	2.51
9.2	9.7	24.3	78	79/49	32	1.54	2.46	2.82
5.2	4.0	16.9	75	76/49	23	1.52	3.29	3.72
7.3	20.4	26.5	43	47/32	21	1.41	2.02	2.32
5.9	22.4	29.8	27	33/23	16	2.36	1.67	1.92
3.3	6.5	13.9	41	52/36	19	2.92	2.11	3.07
4.0	2.5	6.2	33	42/21	46	0.49	0.71	1.63
2.6	8.4	13.8	34	34/22	36	1.75	0.94	2.41
1.9	-1.7	-3.0	55	61/47	-137	2.26	-0.40	4.18
5.6	-5.5	-17.1	54	56/43	-26	1.41	-2.07	1.98
2.5	7.4	8.4	21	26/19	44	2.96	0.48	1.07



Burning Bright

It's hard to rank top-performing companies and not run into General Electric. This industrial behemoth climbed a notch from last year to No. 41. Helping to nudge it upward: sales and earnings gains in 1997 of 15% and 13%, which brought a 50% leap in shareholder returns. But the real story at GE is Chairman Jack Welch's continuing obsession with quality. A new initiative delivered more than \$300 million in operating income last year and could add \$750 million in 1998.

FOOTNOTES TO TABLES APPEAR ON PAGE 123.
ALPHABETICAL INDEX OF COMPANIES
BEGINS ON PAGE 150

THE S&P 500

Business Week's Industry Rankings

MARKET VALUE

SALES

PROFITABILITY

FEB. 27
1998
\$ MIL

TOTAL
RETURN
(1 YEAR)

TOTAL
RETURN
(3 YEARS)

12
MONTHS
1997
\$ MIL

CHANGE
FROM
1996
%

3 YEAR
AVERAGE
CHANGE
%

12
MONTHS
1997
\$ MIL

CHANGE
FROM
1996
%

6 CONSUMER PRODUCTS

INDUSTRY AVERAGE			24939.0	23.9	112.7	9343.6	3	6.9	865.9	10
1	38	GILLETTE	60488.3	35.4	182.6	10062.1	4	20.6	1427.2	50
2	64	NIKE	12752.4	-40.3	150.4	9819.0	26	34.4	787.1	16
3	97	COLGATE-PALMOLIVE	24015.9	58.0	168.4	9056.7	4	5.9	740.4	17
4	106	CLOROX	9073.6	48.1	212.0	2652.7y	13	11.8	263.9	12
5	107	PROCTER & GAMBLE	113885.3	42.7	169.0	36715.0	4	4.7	3625.0	12
6	119	COCA-COLA	169738.6	12.4	157.9	18868.0	1	5.1	4129.0	18
7	127	ECOLAB	3729.2	52.8	162.2	1640.4	10	10.8	134.0	18
8	136	MAYTAG	4273.9	113.1	193.7	3407.9	14	0.2	183.5	33
9	186	LIZ CLAIBORNE	3405.3	23.6	224.2	2412.6	9	4.0	184.6	19
10	208	AVON PRODUCTS	9298.4	21.9	170.5	5079.4	6	6.1	338.8	7
11	213	PHILIP MORRIS	105443.7	0.0	144.4	56114.0	3	1.6	6310.0	0
12	243	PEPSICO	55370.5	21.4	111.9	20917.0	3	-12.4	1491.0	58
13	252	VF	5877.6	41.2	99.7	5222.2	2	1.6	350.9	17
14	287	BROWN-FORMAN	3829.3	28.6	85.0	1642.4	4	5.0	180.6	9
15	289	ARMSTRONG WORLD INDUSTRIES	3184.4	17.7	83.8	2198.7	2	2.0	185.0	12
16	292	ADOLPH COORS	1158.0	48.2	106.9	1822.2	5	3.2	82.3	89
17	293	ANHEUSER-BUSCH	22966.0	8.1	82.6	11066.2	2	-2.0	1179.2	2
18	306	ALBERTO-CULVER	1729.4	7.1	119.2	1794.6	8	13.7	78.5	3
19	323	UST	6530.2	23.3	37.2	1401.7x	2	4.5	439.1	-5
20	338	TANDY	4636.9	80.8	108.3	5372.2	-15	3.3	186.9	NM
21	357	CIRCUIT CITY STORES	3813.6	26.6	80.8	7693.2	8	14.0	123.2	-18
22	363	SEAGRAM	13104.6	-2.3	29.2	12347.0	-7	33.6	336.0	-5
23	423	REEBOK INTERNATIONAL	1755.4	-33.6	-13.5	3643.6	5	3.2	135.1	-3
24	451	WHIRLPOOL	5011.7	36.1	32.6	8617.0y	1	2.1	-46.0	NM
25	475	RUSSELL	989.3	-27.7	-6.0	1228.2	-1	4.2	54.4	-33
26	494	FRUIT OF THE LOOM	2351.9	-21.2	37.4	2139.9	-13	-1.9	-385.4	NM

7 CONTAINERS & PACKAGING

INDUSTRY AVERAGE			3626.3	18.2	78.7	4177.0	5	6.6	84.4	-24
1	51	OWENS-ILLINOIS	5389.1	58.2	265.5	4658.5	21	8.6	272.4	43
2	193	AVERY DENNISON	5202.0	29.3	187.5	3345.7	4	5.2	204.8	16
3	290	BEMIS	2386.9	11.3	77.2	1877.2	13	10.3	107.6	6
4	315	CROWN CORK & SEAL	6931.3	-1.2	32.6	8494.6	2	27.6	301.6	6
5	397	BALL	985.1	33.1	5.9	2388.5	9	-4.1	58.3	345
6	458	TEMPLE-INLAND	3372.4	10.0	31.0	3625.4	5	6.5	50.8	-62
7	493	STONE CONTAINER	1117.1	-13.5	-49.0	4849.1	-6	-8.3	-404.4	NM

8 DISCOUNT & FASHION RETAILING

INDUSTRY AVERAGE			14572.8	42.8	115.3	18181.7	12	12.4	560.2	15
1	17	GAP	17659.0	102.3	326.9	6507.8	23	20.4	533.9	18
2	21	TJX	6288.1	84.8	509.2	7389.1	10	31.9	306.6	43
3	44	HOME DEPOT	46721.4	73.7	116.3	24155.7	24	24.8	1160.0	24
4	53	DAYTON HUDSON	16923.8	92.7	247.8	27757.0y	9	9.1	802.0	69

INVESTMENT DATA								
NET MARGIN 1996	RETURN ON INVESTED CAPITAL	RETURN ON COMMON EQUITY	RECENT SHARE PRICE \$	12-MONTH HIGH/LOW \$	P-E RATIO	D.V. DENG. YIELD	EARNINGS PER SHARE 1997	ESTIMATED EARNINGS PER SHARE 1998
3.7	20.3	28.2	52	57/37	30	1.66	1.74	2.46
0.8	21.6	28.0	108	110/72	43	0.80	2.49	3.04
3.7	20.5	22.8	44	73/38	17	1.09	2.65	2.27
7.3	15.6	33.4	81	82/49	36	1.36	2.27	2.74
0.0	15.5	26.5	88	89/55	35	1.46	2.53	2.75
9.2	21.1	29.1	85	85/57	35	1.19	2.43	2.73
3.7	50.2	56.7	69	73/50	42	0.87	1.64	1.68
7.6	19.6	25.0	29	29/18	29	1.32	1.00	1.16
4.6	13.7	29.8	45	46/20	24	1.42	1.87	2.35
7.0	17.7	17.7	50	58/38	19	0.90	2.63	2.98
5.6	102.6	149.3	70	78/51	28	1.93	2.54	2.96
1.6	22.6	42.3	44	48/37	17	3.68	2.58	3.24
4.6	15.0	23.5	37	41/28	38	1.37	0.95	1.38
5.8	14.3	18.2	48	48/32	18	1.67	2.70	2.94
0.5	21.4	22.8	56	56/44	22	2.02	2.56	2.88
7.6	14.5	22.6	79	80/62	17	2.24	4.50	5.78
2.5	9.2	11.0	31	41/19	14	1.92	2.16	1.99
0.6	14.4	28.5	47	48/39	20	2.22	2.36	2.51
4.6	11.7	15.1	30	33/25	24	0.79	1.29	1.41
3.8	88.6	111.0	35	37/26	15	4.57	2.37	2.56
1.5	14.0	17.1	45	46/24	27	0.90	1.63	2.12
2.1	6.1	7.8	39	46/31	31	0.36	1.24	1.47
2.7	2.6	3.8	38	42/30	41	1.74	0.92	0.81
4.0	11.0	26.6	31	52/26	13	NA	2.32	2.46
1.7	-1.3	-2.6	67	70/45	-108	2.04	-0.62	4.07
5.6	5.3	8.3	27	38/24	18	2.07	1.47	1.73
5.0	-19.8	-46.7	32	45/23	-6	NA	-5.18	1.89
2.8	4.9	5.8	42	47/31	44	1.89	0.94	1.95
5.0	5.7	20.2	38	43/23	19	NA	2.01	2.28
5.5	16.5	24.5	51	55/34	26	1.66	1.93	2.26
5.1	10.9	16.8	45	48/34	23	1.95	2.00	2.28
3.4	3.8	7.8	54	59/44	25	1.85	2.15	2.86
0.6	5.1	8.8	33	39/25	19	1.84	1.74	2.10
3.8	1.1	2.5	60	69/50	66	2.15	0.90	2.53
2.4	-9.0	-95.7	11	18/10	-3	NA	-4.16	-0.68
3.0	9.9	15.2	44	48/28	24	1.14	1.86	2.29
3.6	27.1	36.2	45	46/20	34	0.45	1.30	1.56
3.2	21.8	26.5	39	40/21	22	0.51	1.75	1.99
4.8	13.8	16.3	64	69/35	41	0.31	1.55	2.02
1.9	8.8	18.8	77	80/40	23	0.93	3.40	3.81



Retail Rising

At last, some good news for retailers. Gap, Home Depot, and TJX, which owns T.J. Maxx and Marshalls, all made it into the top 50. That's a stand-out performance in an industry where 10 of the 22 companies languish in the bottom half of our overall S&P 500 rankings. It's also a far better showing than last year, when none made it into the elite 50. What do the three industry stars have in common? Carefully honed brand identities and brisk expansion.

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THE S&P 500

Business Week's Industry Rankings

			MARKET VALUE			SALES			PROFITABILITY	
			1997 \$ MIL	RET. % (1 YEAR)	TOTAL RETURN (3 YEARS)	12 MONTHS 1997 \$ MIL	CHANGE FROM 1996 %	3 YEAR AVERAGE CHANGE %	12 MONTHS 1997 \$ MIL	CHANGE FROM 1996 %
5	62	COSTCO	10472.7	88.0	258.7	22420.8y	12	9.8	378.3	64
6	109	WAL-MART STORES	104014.7	74.5	99.8	117958.0	12	12.6	3526.0	15
7	117	LOWE'S	10245.1	63.8	76.9	10136.9	18	18.7	357.5	22
8	125	FEDERATED DEPARTMENT STORES	9834.9	34.4	113.1	15668.3y	3	21.1	574.6	116
9	161	CONSOLIDATED STORES	3469.3	43.3	238.2	4055.3	19	53.4	85.9	-45
10	196	AUTOZONE	4600.7	21.0	14.2	2797.6	19	21.5	204.6	20
11	246	J.C. PENNEY	17667.9	50.1	86.0	30546.0y	30	11.5	566.0	0
12	248	SEARS, ROEBUCK	20776.1	1.8	123.4	41469.0	8	8.0	1188.0	-7
13	259	MAY DEPARTMENT STORES	14047.9	32.7	97.0	12352.0y	7	0.8	779.0	4
14	275	NORDSTROM	4433.5	61.0	40.4	4960.2y	8	7.6	186.2	26
15	330	TOYS 'R' US	7454.9	2.9	-5.8	11037.8	11	7.7	490.1	15
16	349	WOOLWORTH	3204.7	11.8	55.7	6624.0	-6	-7.8	213.0	10
17	355	LIMITED	7902.2	57.1	76.6	9188.8	6	8.1	217.4	-50
18	371	MERCANTILE STORES	2418.6	38.9	68.7	3143.8y	4	3.6	129.7	7
19	374	DILLARD'S	3957.2	18.8	31.2	6632.0y	6	4.7	258.0	8
20	384	PEP BOYS-MANNY, MOE & JACK	1569.2	-21.4	-20.0	1998.6b	11	13.9	100.1b	3
21	435	KMART	6465.0	11.6	9.5	32183.0	2	-1.5	249.0	8
22	486	CHARMING SHOPPES	474.6	-2.1	-26.4	1016.5	0	-7.3	19.3	NM

9 ELECTRICAL & ELECTRONICS

INDUSTRY AVERAGE			13325.3	12.4	84.1	6103.5	9	11.3	559.8	28
1	4	INTEL	146729.6	28.6	352.5	25070.0	20	29.5	6945.0	35
2	128	THOMAS & BETTS	3118.0	32.2	85.0	2114.7	7	28.4	154.9	159
3	134	EMERSON ELECTRIC	28294.2	30.3	107.0	12639.5	11	12.3	1149.3	10
4	138	THERMO ELECTRON	6204.4	20.1	94.8	3558.3	21	27.4	239.3	25
5	162	EATON	7406.5	34.3	105.4	7563.0	9	7.1	464.0	33
6	166	HONEYWELL	10087.7	13.4	131.0	8027.5	10	9.7	471.0	17
7	197	RAYCHEM	3684.7	1.7	120.1	1815.5	5	6.6	245.7	14
8	238	HARRIS	4051.6	40.7	140.7	3917.5	5	4.7	220.2	17
9	249	ANDREW	2442.0	-26.3	60.7	874.9	7	14.6	110.5	9
10	255	KLA-TENCOR	3878.5	13.3	59.2	1167.3	6	57.1	139.4	-18
11	280	AMP	9722.2	14.9	25.8	5745.0	5	9.1	457.5	59
12	291	COOPER INDUSTRIES	6903.4	29.2	57.0	5288.8	0	5.5	394.6	25
13	320	MICRON TECHNOLOGY	7022.6	-10.0	7.6	3742.0	17	22.2	321.2	12
14	324	RAYTHEON	13899.3	27.1	75.4	13673.5	11	10.4	526.8	-31
15	336	NATIONAL SERVICE INDUSTRIES	2385.7	47.9	127.2	2011.8	-1	1.9	109.1	6
16	344	PERKIN-ELMER	3552.6	1.7	166.8	1309.5	8	8.3	64.0	13
17	350	TEKTRONIX	2252.4	37.4	103.0	2033.1	10	13.2	71.1	-29
18	364	TEXAS INSTRUMENTS	22590.9	50.6	204.0	9750.0	-2	-4.4	302.0	NM
19	372	MOTOROLA	33205.3	1.0	-1.1	29794.0	7	9.5	1180.0	2
20	375	ROCKWELL INTERNATIONAL	12251.3	9.7	106.8	7888.0	6	-10.4	474.0	5
21	396	LSI LOGIC	3356.0	-27.1	-13.1	1290.3	4	11.1	160.7	9
22	403	GENERAL SIGNAL	2043.4	-5.1	22.2	1954.6	-5	8.8	131.0	-2
23	404	NATIONAL SEMICONDUCTOR	3921.1	-10.7	40.4	2582.1	3	3.1	298.6	NM

INVESTMENT DATA								
NET MARGIN 1996	RETURN ON INVESTED CAPITAL	RETURN ON COMMON EQUITY	RECENT SHARE PRICE \$	12-MONTH HIGH/LOW \$	P-E RATIO	DIVIDEND YIELD	EARNINGS PER SHARE 1997	ESTIMATED EARNINGS PER SHARE 1998
1.2	10.5	14.7	49	51/26	28	NA	1.75	1.96
2.9	12.4	20.1	46	48/26	30	0.58	1.56	1.75
3.4	9.8	13.7	58	62/34	29	0.38	2.05	2.45
1.7	6.3	10.9	47	49/32	18	NA	2.58	2.98
4.6	6.6	12.4	41	50/28	53	NA	0.77	2.06
7.3	15.3	18.1	30	33/22	23	NA	1.33	1.53
2.4	3.6	7.3	71	73/45	34	3.03	2.10	3.94
3.3	6.6	22.0	53	65/39	18	1.74	2.99	3.42
6.5	10.4	20.0	61	63/44	20	2.09	3.11	3.45
3.2	10.3	12.5	57	68/36	24	0.98	2.40	2.79
4.3	9.7	11.9	26	37/25	15	NA	1.70	2.14
2.8	12.3	18.5	24	29/18	15	NA	1.57	1.87
5.0	7.1	9.3	29	32/17	37	1.79	0.79	1.43
4.0	7.3	8.2	66	69/46	19	1.82	3.53	3.82
3.8	6.2	9.2	36	45/29	15	0.45	2.31	2.70
5.4	6.6	11.8	26	36/22	16	0.94	1.58	1.53
0.7	2.7	4.6	13	15/10	26	NA	0.51	0.87
-0.7	3.4	4.4	4	7/4	25	NA	0.18	0.22
7.8	10.9	17.1	50	62/37	25	1.50	2.02	2.62
4.7	31.9	32.6	90	102/64	23	0.13	3.87	4.33
3.0	10.5	15.8	57	59/40	20	1.98	2.81	3.21
9.1	18.5	20.3	64	65/45	25	1.85	2.59	2.79
6.5	5.4	13.4	41	45/28	29	NA	1.41	1.76
5.0	12.8	20.8	96	103/68	16	1.83	5.93	7.12
5.5	13.3	20.0	79	81/65	21	1.41	3.71	4.22
2.5	24.4	29.3	43	50/30	16	0.74	2.75	2.71
5.1	9.5	13.6	51	52/36	18	1.73	2.75	2.90
2.4	20.2	22.1	28	41/20	23	NA	1.22	1.42
5.5	12.2	12.2	46	77/33	29	NA	1.59	2.24
5.2	14.8	15.6	44	57/33	21	2.44	2.08	2.40
6.0	10.9	15.6	56	59/41	17	2.35	3.26	3.53
8.9	8.5	11.1	33	60/22	23	NA	1.47	-0.04
6.2	5.6	10.5	59	61/42	27	1.36	2.20	3.77
5.1	16.6	17.3	55	56/37	23	2.24	2.44	2.63
4.7	12.1	14.1	73	86/56	52	0.93	1.42	2.99
5.4	7.9	9.4	45	46/32	31	1.08	1.43	3.05
-0.5	4.2	5.1	58	71/36	76	0.59	0.76	2.48
4.1	7.9	9.0	56	91/54	29	0.86	1.94	2.82
6.1	10.0	10.3	61	70/44	24	1.69	2.47	3.16
1.9	9.4	10.3	24	47/19	21	NA	1.12	1.13
6.5	15.6	20.8	41	53/36	16	2.66	2.60	2.73
-5.9	12.8	14.7	24	43/22	13	NA	1.89	1.74



Chip Dip

There aren't many companies that have to apologize for sales gains of 20% and earnings gains of 35%. But for Intel, those 1997 numbers were subpar and helped topple the chip-maker to No. 4, from the top spot it held a year ago. And there may be worse to come. In March, the company warned that it would miss first-quarter sales projections by 10%. The problem: PC sales growth is slowing, pushing chip prices down. Still, with an 85% share of the world micro-processor market, Intel's situation is far from dire.

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THE S&P 500

Business Week's Industry Rankings

			MARKET VALUE			SALES			PROFITABILITY	
			FEB 27 1998 \$ MIL.	TOTAL RETURN (1 YEAR)	TOTAL RETURN (3 YEARS)	12 MONTHS 1997 \$ MIL.	CHANGE FROM 1996 %	3-YEAR AVERAGE CHANGE %	12 MONTHS 1997 \$ MIL.	CHANGE FROM 1996 %
24	453	MILLIPORE	1638.1	-11.7	46.5	758.9	23	14.0	-38.8	NM
25	474	ADVANCED MICRO DEVICES	3348.8	-33.6	-22.6	2356.4	21	0.6	-21.1	NM
26	491	GENERAL INSTRUMENT	2467.2	12.5	-15.4	1764.1	0	-7.3	-16.1	NM

10 Food

INDUSTRY AVERAGE			12747.5	34.8	111.8	11128.2	3	2.5	269.3	-29
1	98	HERSHEY FOODS	9529.8	50.5	188.6	4302.2	8	6.3	336.3	23
2	131	CAMPBELL SOUP	26360.6	31.0	171.3	8057.0	3	5.0	927.0	34
3	175	SUPERVALU	2862.5	56.8	103.3	16793.4	2	0.8	232.1	36
4	207	KROGER	10746.1	59.8	221.9	26567.3	6	5.0	444.0	26
5	218	PIONEER HI-BRED INTERNATIONAL	6822.3	52.2	221.5	1773.0	3	6.6	237.0	4
6	232	SYSCO	8014.5	37.1	74.0	14779.4	5	8.8	316.4	9
7	235	WM. WRIGLEY JR.	8857.1	27.8	78.9	1954.2	6	6.8	271.6	18
8	247	RALSTON PURINA	10434.4	22.8	124.3	4543.3	5	-19.3	371.6	24
9	265	ALBERTSON'S	11503.6	35.1	60.0	14689.5	7	3.0	516.8	5
10	277	CONAGRA	14161.8	14.4	95.0	23828.5	-1	-0.5	652.4	199
11	294	KELLOGG	17506.1	26.5	68.9	6830.1	2	0.7	564.0	6
12	304	WINN-DIXIE STORES	8017.5	72.5	109.1	13382.3	2	5.5	213.4	-8
13	308	BESTFOODS	15163.5	35.0	125.4	8400.4	-1	3.8	428.8	-23
14	309	GENERAL MILLS	11380.6	12.9	59.0	5788.4	4	5.0	389.8	-13
15	341	H.J. HEINZ	20580.7	39.8	135.6	9180.0	-3	6.3	390.8	-44
16	365	ARCHER DANIELS MIDLAND	12821.7	26.9	41.2	14789.4	9	6.5	454.4	-9
17	385	AMERICAN STORES	6884.4	13.7	116.7	19138.9	2	1.5	280.6	-2
18	408	SARA LEE	26734.1	47.3	129.2	19751.0	3	5.7	-567.0	NM
19	410	GREAT ATLANTIC & PACIFIC TEA	1164.3	2.1	62.8	10106.8	0	-0.7	73.3	-3
20	454	GIANT FOOD	2268.7	12.0	63.1	4021.6	2	3.3	52.5	-53
21	463	QUAKER OATS	7460.7	53.5	82.3	5015.7	-4	-6.3	-930.9	NM
INC	INC	UNILEVER NV	41170.9	35.2	128.2	NA	NA	NA	NA	NA

11 FUEL

INDUSTRY AVERAGE			22634.5	24.5	97.5	18622.1	-2	10.8	1214.8	6
1	18	SCHLUMBERGER	37640.7	53.4	180.0	10647.6	19	16.8	1295.7	52
2	43	HALLIBURTON	12213.5	47.2	174.7	8818.6y	19	17.8	454.4	51
3	66	HELMERICH & PAYNE	1454.7	39.0	131.6	536.5	29	19.7	93.2	66
4	67	ROWAN	2440.6	44.6	351.0	695.3	22	17.1	156.4	155
5	124	TEXACO	29492.8	14.8	96.6	46667.0y	3	14.2	2664.0	32
6	154	WESTERN ATLAS	4139.4	58.3	134.0	1658.2	17	11.5	91.8	31
7	159	EXXON	157201.1	31.3	122.2	122089.0y	2	7.4	8460.0	13
8	160	CHEVRON	53114.9	25.7	88.6	35009.0	-7	6.3	3256.0	25
9	171	ATLANTIC RICHFIELD	24938.7	27.5	62.3	18684.0	0	8.5	1889.0	14
10	172	UNOCAL	9291.1	0.0	42.7	6064.0y	14	-6.7	669.0	47
11	194	APACHE	3075.1	5.4	39.7	1176.3y	20	26.8	154.9	28
12	221	ASHLAND	4176.6	34.6	86.8	13352.0	7	10.6	221.0	73
13	237	ANADARKO PETROLEUM	3860.5	15.2	49.4	673.2	18	13.5	107.3	7
14	256	ROYAL DUTCH PETROLEUM	116463.1	28.7	116.0	76893.0	0	11.2	4881.0	-13

INVESTMENT DATA								
NET GAIN 1996	RETURN ON INVESTED CAPITAL	RETURN ON COMMON EQUITY	PERCENT SHARE PRICE \$	12-MONTH HIGH/LOW \$	P-E RATIO	DIVIDEND YIELD	EARNINGS PER SHARE 1997	ESTIMATED EARNINGS PER SHARE 1998
7.1	-8.9	-26.0	38	52/30	-42	1.06	-0.89	2.04
3.5	-0.8	-1.0	24	49/17	-157	NA	-0.15	0.36
5.5	-1.3	-1.3	17	28/13	-152	NA	-0.11	0.59
3.5	8.5	15.1	56	60/39	41	1.67	1.38	2.40
6.8	18.6	43.4	67	68/44	30	1.32	2.23	2.58
8.8	33.7	62.5	58	59/44	29	1.45	2.01	2.11
1.0	9.4	19.4	48	49/28	13	2.18	3.61	3.08
1.4	16.8	NM	42	44/24	25	NA	1.69	1.96
3.2	18.3	18.7	104	109/58	37	1.00	2.78	3.48
2.1	14.2	22.7	47	49/33	26	1.53	1.83	1.95
2.4	27.6	27.6	76	82/56	33	1.00	2.34	2.58
6.9	9.4	18.1	101	102/75	30	1.18	3.37	3.72
3.6	15.2	22.7	47	50/31	24	1.37	1.99	2.32
0.9	11.9	25.5	30	39/26	21	2.08	1.42	1.58
8.0	23.4	56.5	43	51/32	31	2.11	1.36	1.86
1.8	15.1	15.7	54	63/32	38	1.89	1.43	1.51
6.6	11.0	21.2	105	109/77	37	1.71	2.85	4.48
8.1	19.6	100.2	72	78/58	29	2.95	2.45	3.62
7.4	8.0	16.0	56	60/38	54	2.24	1.04	2.39
3.7	4.9	7.0	22	25/16	28	0.89	0.81	1.18
1.5	5.3	12.6	25	28/19	25	1.43	1.01	1.34
5.0	-12.0	-24.5	57	60/39	-44	1.63	-1.29	2.32
0.8	3.9	7.9	30	36/23	16	1.31	1.91	2.31
2.9	5.0	6.0	36	38/28	42	2.15	0.87	1.69
4.8	-80.5	-347.1	54	56/36	-8	2.12	-6.80	2.21
NA	NA	NA	64	66/45	NA	1.55	NA	2.62
6.0	10.0	16.5	53	62/41	20	2.01	2.65	2.79
9.5	16.7	19.4	76	94/49	30	0.99	2.52	3.41
4.1	15.2	18.6	47	63/31	27	1.07	1.75	2.38
3.5	11.6	11.6	29	46/21	16	0.97	1.85	1.99
0.7	17.2	24.0	28	44/17	16	NA	1.76	2.64
4.4	15.0	20.4	56	63/49	11	3.23	4.87	3.19
4.9	5.8	10.4	76	94/57	46	NA	1.65	2.60
6.3	16.7	19.5	64	67/49	19	2.57	3.37	2.99
6.9	15.1	19.1	81	89/62	16	3.02	5.03	4.29
8.9	13.7	21.7	78	87/62	14	3.67	5.41	4.54
8.6	13.4	28.9	38	45/33	14	2.12	2.65	2.04
2.4	5.3	9.6	34	45/30	20	0.82	1.71	1.49
1.0	5.5	10.6	56	57/39	19	1.98	2.90	3.55
7.7	5.5	10.0	65	77/51	36	0.47	1.78	1.85
7.3	11.9	13.5	54	59/42	24	2.04	2.30	2.60



Pumped Up

From Kazakhstan to the Gulf of Mexico, demand for oil rigs and exploration services is booming. That helped power oil-service giants Schlumberger and Halliburton onto the BW 50 and to the top of their peer group. Oil-field spending climbed 20% for the third year in a row in 1997, and Big Oil is passing more of the work of finding and drilling wells to service providers. But that could end if crude oil prices keep falling.

FOOTNOTES TO TABLES APPEAR ON PAGE 123.
ALPHABETICAL INDEX OF COMPANIES
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THE S&P 500

Business Week's Industry Rankings

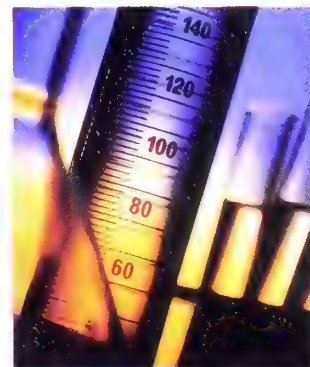
			MARKET VALUE			SALES			PROFITABILITY	
			FEB 27 1998 \$ M	TOTAL RETURN 1 YEAR	TOTAL RETURN (3 YEARS)	12 MONTHS 1997 \$ MIL	CHANGE FROM 1996 %	3 YEAR AVERAGE CHANGE %	12 MONTHS 1997 \$ MIL	CHANGE FROM 1996 %
15	258	DRYX ENERGY	2686.8	25.6	121.2	1197.0y	4	4.4	172.0	6
16	261	PHILLIPS PETROLEUM	12915.4	22.9	61.8	15210.0	-3	8.6	959.0	-26
17	267	USX-MARATHON GROUP	9963.8	36.9	133.8	15668.0x	-4	18.1	456.0	-32
18	270	MOBIL	56711.3	20.0	82.2	65709.0z	-19	5.7	3272.0	10
19	286	AMOCO	41389.6	3.9	58.9	31910.0	-1	8.1	2720.0	-4
20	317	BAKER HUGHES	6934.9	19.2	123.2	3992.1	26	17.0	137.0	-30
21	334	BURLINGTON RESOURCES	7907.7	4.1	20.8	2000.0	-9	32.9	319.0	-5
22	340	COASTAL	6747.8	39.4	128.1	9611.1	-19	-0.5	392.1	-22
23	346	SUN	2857.4	51.0	53.9	10531.0z	-7	13.6	263.0	NM
24	353	UNION PACIFIC RESOURCES GROUP	5674.2	-7.0	NA	1905.7	4	14.7	333.0	4
25	358	PENNZOIL	3177.6	18.7	55.1	2654.3y	7	1.0	180.3	35
26	393	KERR-McGEE	3223.0	10.8	45.7	1711.4	-11	2.8	193.8	-12
27	461	AMERADA HESS	5414.6	10.0	24.7	8340.0y	-7	9.4	7.5	-99
28	466	OCCIDENTAL PETROLEUM	8659.6	4.1	46.5	8016.0	0	-6.7	217.0	-58

12 HEALTH CARE

INDUSTRY AVERAGE			27538.8	36.2	155.9	7329.2	12	16.1	675.5	-7
1	11	SCHERING-PLOUGH	55754.2	100.7	310.7	6778.0	20	14.0	1444.0	19
2	12	PFIZER	114453.1	94.0	348.6	12504.0	11	15.8	2213.0	15
3	15	MERCK	153373.8	38.3	220.8	23636.9	19	16.7	4614.1	19
4	22	BRISTOL-MYERS SQUIBB	99614.7	53.8	254.6	16701.0	11	11.5	3205.0	12
5	28	GUIDANT	10539.7	117.6	708.6	1328.2	27	15.2	150.0	187
6	46	HEALTHSOUTH	9234.8	29.6	168.9	3017.3	17	37.7	330.6	74
7	48	RITE AID	8343.8	53.3	178.7	10841.6	89	33.3	251.9	55
8	60	WARNER-LAMBERT	39809.6	77.5	306.9	8179.8	13	7.8	869.5	11
9	61	JOHNSON & JOHNSON	100813.0	32.7	178.6	22629.0	5	13.1	3303.0	14
10	65	BOSTON SCIENTIFIC	11628.4	-12.9	176.3	1872.3	21	29.6	331.0	12
11	76	WALGREEN	18161.1	71.8	222.7	13794.0	14	13.2	448.0	17
12	87	CARDINAL HEALTH	8978.7	33.1	149.5	11616.6	14	18.7	224.2	64
13	88	AMERICAN HOME PRODUCTS	60868.9	48.5	186.9	14196.0	1	15.4	2043.1	8
14	95	MEDTRONIC	24891.2	66.8	260.0	2560.2y	7	16.3	442.8	-13
15	96	ABBOTT LABORATORIES	57300.8	32.3	123.3	11883.5	8	9.2	2094.5	11
16	130	BIOMET	3331.7	98.2	86.3	605.3	9	14.3	116.2	15
17	144	MANOR CARE	2389.8	43.5	101.2	1393.5	18	8.6	129.0	83
18	189	UNITED HEALTHCARE	11411.1	20.8	41.4	11794.5y	17	49.1	459.7	29
19	220	SIGMA-ALDRICH	3962.0	30.0	121.8	1127.1	9	9.6	166.1	12
20	227	AMGEN	13982.5	-12.3	54.0	2401.0	7	13.6	644.3	-5
21	228	HUMANA	4166.9	33.9	8.2	7880.0y	18	30.4	173.0	1342
22	260	BECTON, DICKINSON	7773.4	29.0	151.2	2856.4	3	3.0	306.3	3
23	283	CVS	12753.6	61.4	178.9	12738.2	16	12.5	37.3	-89
24	307	TENET HEALTHCARE	11416.8	37.6	140.7	9348.5	15	50.3	-18.0	NM
25	311	ELI LILLY	73007.3	52.6	320.9	8517.6	16	13.7	-385.1	NM
26	319	BAXTER INTERNATIONAL	15845.3	24.3	113.8	6138.0	13	10.7	300.0	-48
27	361	ALLERGAN	2281.0	3.8	27.3	1149.0	-1	6.8	128.3	66

RANK 1996	PERF. ON INVESTED CAPITAL	RETURN ON COMMON EQUITY	INVESTMENT DATA					
			RECENT SHARE PRICE \$	12-MONTH HIGH/LOW \$	P/E RATIO	DIVIDEND YIELD	EARNINGS PER SHARE 1997	ESTIMATED EARNINGS PER SHARE 1998
4.2	13.4	159.3	25	31/17	16	NA	1.63	1.22
3.3	11.7	20.3	49	52/37	14	2.78	3.61	3.16
4.1	7.4	12.6	35	39/26	22	2.43	1.58	2.15
3.6	13.6	16.5	72	78/60	18	3.16	4.00	4.09
3.8	12.6	16.7	85	99/77	15	3.53	5.50	4.78
5.2	3.8	5.2	41	50/33	50	1.12	0.82	2.11
5.2	6.7	10.6	45	54/39	25	1.23	1.79	1.79
4.2	5.4	11.8	64	65/44	18	0.63	3.49	4.03
2.5	9.4	14.6	40	46/24	15	2.50	2.70	3.15
7.5	11.1	18.9	22	30/21	17	0.89	1.33	1.23
5.4	5.4	15.8	67	84/45	18	1.49	3.76	3.59
2.4	9.7	13.5	68	72/56	17	2.66	4.04	4.16
7.4	0.1	0.2	59	65/47	738	1.02	0.08	1.54
5.4	1.3	2.4	26	31/22	66	3.91	0.39	1.67

4.2	13.3	21.1	57	61/36	45	1.12	1.25	2.22
4.4	52.2	53.4	76	78/35	39	1.00	1.95	2.31
7.1	27.1	29.9	89	91/42	52	0.86	1.70	2.10
9.6	29.3	36.0	128	131/80	34	1.41	3.74	4.45
3.9	39.1	46.3	100	105/57	32	1.56	3.14	3.70
5.0	20.8	28.1	73	75/29	73	0.07	0.97	1.99
7.4	8.5	17.1	27	29/18	30	NA	0.91	1.18
2.8	4.7	8.9	32	34/21	32	1.33	1.00	1.51
0.9	18.7	31.9	146	158/81	47	1.31	3.11	4.35
3.4	24.6	27.1	75	76/51	31	1.17	2.41	2.83
9.0	32.1	33.6	60	78/41	36	NA	1.66	2.05
3.2	18.5	18.5	37	37/20	40	0.68	0.91	1.02
1.3	12.8	15.2	82	86/52	41	0.15	2.01	2.49
3.4	15.2	27.4	94	97/57	30	1.84	3.11	3.79
1.1	22.6	22.8	53	59/29	56	0.41	0.95	1.54
7.1	36.2	43.3	75	76/53	28	1.60	2.72	3.05
3.1	19.2	19.2	30	31/15	29	0.37	1.04	1.29
5.0	10.9	17.7	38	38/22	19	0.23	2.03	1.98
3.5	9.0	8.6	61	63/42	27	0.05	2.26	2.77
4.3	16.1	16.1	40	43/27	24	0.71	1.62	1.88
0.4	27.2	30.1	53	69/45	23	NA	2.35	3.04
0.2	8.4	11.9	25	26/18	24	NA	1.05	1.31
0.7	14.8	21.9	64	67/42	27	0.91	2.33	2.73
3.1	0.9	1.1	74	75/44	529	0.59	0.14	2.51
4.4	-0.2	-0.5	37	38/23	-622	NA	-0.06	2.04
0.7	-5.8	-8.8	66	72/39	-188	1.22	-0.35	1.97
0.6	6.0	12.2	57	60/42	53	2.06	1.06	2.62
5.7	13.0	15.2	35	37/26	18	1.49	1.95	1.90



Hiccups?

The health of the health-care sector has been decidedly mixed. Although seven high-performing companies make it one of the best-represented industries in the top 50, that's still way off the 13 companies that made the list last year. Gone is last year's No. 50, scandal-plagued Columbia/HCA, but strong sales for Guidant's medical devices sent it zooming up to No. 28 from No. 344. Schering-Plough, with record sales and earnings in 1997, climbed to the top of the group and to No. 11 in the overall rankings. If the industry rolls out new drugs as scheduled, expect more standouts next year.

FOOTNOTES TO TABLES APPEAR ON PAGE 123.
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THE S&P 500

Business Week's Industry Rankings

			MARKET VALUE			SALES			PROFITABILITY	
			FEB. '97 1996 \$ MIL	TOTAL RET. '96-97 (1 YEAR)	TOTAL PEILF. '96-97 (3 YEARS)	12 MONTHS 1997 \$ MIL	CHANGE FROM 1996 %	3 YEAR AVERAGE CHANGE	12 MONTHS 1997 \$ MIL	CHANGE FROM 1996 %
28	387	U.S. SURGICAL	2323.9	-26.1	47.4	1172.1	5	8.5	94.1	-14
29	392	LONGS DRUG STORES	1228.4	25.2	115.5	2952.9	4	5.1	57.7	-2
30	402	ST. JUDE MEDICAL	3351.5	-9.0	51.0	994.4	13	37.6	54.7	-10
31	427	C.R. BARD	1986.9	29.7	39.1	1213.5	2	4.5	72.3	-22
32	437	ALZA	3210.3	30.8	68.0	464.4	12	21.7	-261.1	NM
33	438	BAUSCH & LOMB	2476.1	22.2	47.1	1915.7	-1	1.0	49.4	-41
34	447	PHARMACIA & UPJOHN	20217.7	10.4	79.9	6710.0	-8	-0.2	323.0	-43
35	457	COLUMBIA/HCA HEALTHCARE	17681.4	-35.0	-1.2	18819.0	0	8.7	182.0	-88
36	476	MALLINCKRODT	2833.0	-6.5	24.4	2120.4	15	2.1	-276.1	NM

13 HOUSING & REAL ESTATE

INDUSTRY AVERAGE			4224.3	44.4	104.5	3942.0	8	7.7	219.8	51
1	122	MASCO	8981.1	58.3	132.4	3760.0	16	-4.1	382.4	30
2	187	SHERWIN-WILLIAMS	5778.4	20.3	108.4	4881.1	18	17.3	260.6	14
3	201	CENTEX	2169.4	81.9	191.7	3788.1y	4	5.9	129.8	39
4	262	PPG INDUSTRIES	11540.3	18.9	90.2	7379.0	2	4.9	714.0	-4
5	271	FLEETWOOD ENTERPRISES	1709.8	81.6	129.7	2954.6	2	1.6	101.4	24
6	279	KAUFMAN & BROAD HOME	1013.1	87.3	89.0	1876.3	5	13.5	58.2	NM
7	391	PULTE	965.9	33.8	102.7	2524.0y	6	13.3	49.8	-21
8	439	OWENS CORNING	1636.5	-27.0	-8.0	4373.0	14	9.0	62.0	NM

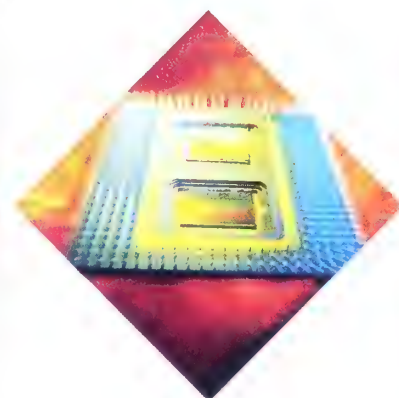
14 LEISURE TIME INDUSTRIES

INDUSTRY AVERAGE			12409.9	27.6	69.8	6685.3	5	12.5	331.1	-10
1	91	WALT DISNEY	75782.0	48.4	113.8	22534.0	6	31.9	1972.0	34
2	103	MARRIOTT INTERNATIONAL	9529.4	44.1	149.1	12034.0	18	12.7	335.0	9
3	146	HILTON HOTELS	7462.6	22.5	76.9	5316.0	35	61.5	250.0	60
4	181	VIACOM	16641.6	38.1	7.3	13206.1	9	20.4	374.5	119
5	191	McDONALD'S	37583.0	26.3	67.4	11408.8	7	10.9	1642.5	4
6	223	MATTEL	12291.9	70.7	142.6	4834.6	7	15.6	289.8	-22
7	229	KING WORLD PRODUCTIONS	1963.0	48.6	58.0	679.9	2	15.8	142.8	1
8	257	AMERICAN GREETINGS	3321.1	50.8	65.8	2208.1	5	6.3	188.7	19
9	348	BRUNSWICK	3160.6	11.3	70.2	3657.4	16	10.5	151.2	-19
10	354	MIRAGE RESORTS	4107.0	-10.0	93.2	1389.0	2	3.3	209.8	2
11	366	HARRAH'S ENTERTAINMENT	2126.3	13.1	-17.0	1619.2	2	5.7	107.5	9
12	367	WENDY'S INTERNATIONAL	2508.7	6.3	44.0	2037.3	7	12.9	130.5	-16
13	412	HASBRO	4792.0	27.5	78.0	3188.6	6	6.0	135.0	-32
14	469	DARDEN RESTAURANTS	2005.6	91.1	NA	3172.1	0	0.9	-68.4	NM
15	471	EASTMAN KODAK	21328.1	-26.0	38.4	14538.0	-9	2.8	5.0	-100
16	484	TRICON GLOBAL RESTAURANTS	4325.6	-1.0d	NA	9681.0	-5	-2.8	-111.0	NM
17	487	POLAROID	2040.3	7.6	59.3	2146.4	-6	-2.0	-126.7	NM

15 MANUFACTURING

INDUSTRY AVERAGE			7166.3	34.5	109.7	5034.5	9	8.1	343.4	16
1	13	APPLIED MATERIALS	13519.6	55.0	219.2	4546.2	15	32.7	697.8	53
2	57	CATERPILLAR	20313.0	39.7	125.0	18925.0	15	9.0	1665.0	22

INVESTMENT DATA								
NET MARGIN 1996	RETURN ON INVESTED CAPITAL	RETURN ON COMMON EQUITY	RECENT SHARE PRICE \$	12-MONTH HIGH/LOW \$	P-E RATIO	DIVIDEND YIELD	EARNINGS PER SHARE 1997	ESTIMATED EARNINGS PER SHARE 1998
8	6.4	7.1	31	45/23	25	0.52	1.21	1.75
1	9.6	9.9	32	34/23	22	1.77	1.47	1.64
9	4.5	5.6	37	43/27	62	NA	0.59	1.61
7	7.9	12.6	35	39/27	28	2.07	1.26	2.00
4	-22.0	-86.7	38	38/25	-12	NA	-3.07	1.44
3	3.1	5.9	45	48/36	50	2.32	0.89	2.41
7	5.0	5.6	40	41/28	65	2.71	0.61	1.64
8	1.0	2.1	27	44/24	100	0.30	0.27	0.99
0	-19.8	-32.6	39	43/35	-10	1.70	-3.86	2.13
0	10.1	20.9	42	45/27	19	1.19	2.19	3.10
1	11.0	17.8	54	55/35	24	1.55	2.30	2.63
5	11.0	16.7	33	34/24	22	1.35	1.50	1.68
6	9.7	13.7	37	38/17	17	0.44	2.14	2.52
3	18.6	28.5	65	68/49	16	2.10	3.94	4.43
8	18.3	20.4	47	47/24	17	1.45	2.77	2.94
4	5.1	15.2	26	29/13	18	1.15	1.45	1.84
7	3.6	6.1	46	46/27	20	0.53	2.27	3.24
4	3.7	NM	31	45/27	26	0.98	1.16	2.97
8	5.3	8.5	42	48/30	40	1.09	1.07	2.04
9	6.5	10.8	112	116/70	39	0.56	2.87	3.20
0	10.4	22.5	76	77/50	31	0.48	2.46	2.97
0	3.8	6.9	30	36/24	32	1.07	0.94	1.44
4	1.4	2.5	48	49/25	54	NA	0.89	0.02
7	11.2	17.5	55	56/42	24	0.61	2.29	2.63
2	11.2	15.3	42	43/23	45	0.66	0.94	1.98
2	17.4	17.4	27	30/17	14	NA	1.90	1.93
6	11.9	13.8	46	47/29	18	1.58	2.50	2.64
9	7.7	11.7	32	37/26	21	1.58	1.51	2.45
2	8.4	14.4	23	30/20	21	NA	1.09	1.21
2	6.4	14.6	21	23/16	20	NA	1.06	1.37
2	7.9	10.8	22	28/20	22	1.11	0.97	1.18
7	7.3	7.3	36	37/23	36	0.88	1.02	1.98
5	-5.0	-6.4	14	14/7	-30	0.59	-0.45	0.75
3	0.1	0.1	66	93/53	NM	2.68	0.01	4.13
5	-3.0	-3.1	29	40/25	NA	NA	NA	2.00
7	-12.9	-26.2	46	60/36	-16	1.31	-2.81	2.73
4	12.5	19.9	51	58/35	20	1.62	2.53	3.17
6	18.7	22.5	37	54/22	28	NA	1.32	1.53
3.2	14.7	35.5	55	62/38	12	1.83	4.37	4.50



Lucky 13

With the top of the BW 50 dominated by companies that make and use computer chips, it figures that Applied Materials is highly ranked, too. At No. 13, this California company is the leading manufacturer of the equipment used by Intel and others to turn silicon into semiconductors. Can it stay at the top? That will likely depend on what happens in Asia, where Applied Materials does half its business.

FOOTNOTES TO TABLES APPEAR ON PAGE 123;
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THE S&P 500

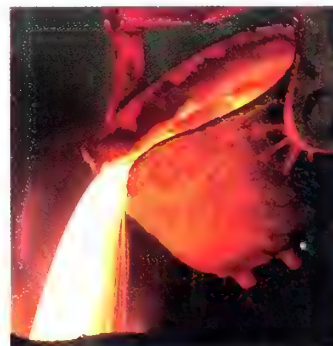
Business Week's Industry Rankings

			MARKET VALUE			SALES			PROFITABILITY	
			FEB. 27 1999 \$ MIL.	TOTAL RET. (%) 1 YEAR	TOTAL RETURN (3 YEARS)	12 MONTHS 1997 \$ MIL.	CHANGE FROM 1996	5 YEAR AVERAGE CHANGE	12 MONTHS 1997 \$ MIL.	CHANGE FROM 1996
3	59	PARKER HANNIFIN	5170.0	61.8	136.7	4360.3	13	15.2	319.9	35
4	75	DOVER	8589.7	55.2	170.7	4547.7	12	13.3	405.4	4
5	80	DEERE	14047.7	34.9	134.0	13241.4y	17	11.7	986.4	19
6	84	ILLINOIS TOOL WORKS	14951.8	43.2	175.5	5220.4	4	15.2	587.0	21
7	118	DRESSER INDUSTRIES	7813.4	50.1	132.1	7489.6y	10	13.3	328.0	25
8	126	CASE	4886.4	25.2	182.1	6024.0y	11	10.5	403.0	15
9	143	INGERSOLL-RAND	7884.3	51.9	136.5	7103.3	6	16.4	380.5	6
10	178	MINNESOTA MINING & MFG.	34528.3	-5.3	75.4	15070.0	6	0.5	2121.0	40
11	179	NEWELL	7298.7	25.6	102.7	3234.3	13	15.9	290.4	13
12	200	TIMKEN	2031.1	24.5	94.0	2617.6	9	10.3	171.4	23
13	203	JOHNSON CONTROLS	4676.7	33.9	139.2	11440.4	15	17.1	231.1	-1
14	219	CINCINNATI MILACRON	1223.8	47.8	54.0	1896.7	10	15.4	80.6	22
15	230	CORNING	9392.5	9.8	58.5	4129.1y	12	-3.3	439.8	28
16	244	SNAP-ON	2587.2	10.8	101.4	1744.1y	13	11.9	150.4	14
17	264	W.R. GRACE	6194.6	55.4	178.4	3312.8	-4	0.6	248.6	16
18	266	HARNISCHFEGER INDUSTRIES	1664.3	-18.1	31.1	3054.6	3	22.3	143.7	18
19	269	AEROQUIP-VICKERS	1629.5	58.6	129.4	2112.3	4	5.8	100.9	-2
20	273	NACCO INDUSTRIES	1060.4	142.5	163.0	2246.9	-1	6.1	61.8	22
21	274	BLACK & DECKER	4777.7	58.9	95.8	4940.5	1	-1.5	227.2	43
22	342	CUMMINS ENGINE	2207.9	12.7	35.7	5625.0	7	5.3	212.0	33
23	343	JOSTENS	912.8	10.9	26.7	742.5	5	0.8	57.2	57
24	409	McDERMOTT INTERNATIONAL	2212.3	79.2	53.8	3482.3	6	4.9	9.2	NM
25	431	RUBBERMAID	4344.1	23.8	-2.4	2399.7	2	3.1	142.5	-6
26	436	BRIGGS & STRATTON	1097.2	3.9	47.5	1334.1	8	-0.7	57.8	-31
27	443	SPRINGS INDUSTRIES	1106.0	28.7	55.0	2226.1	0	2.2	69.0	-22
28	459	STANLEY WORKS	4268.2	26.5	155.9	2669.5	0	2.0	-41.9	NM
29	462	TUPPERWARE	1640.2	-38.2	NA	1229.3	-10	-1.0	82.0	-53
30	464	FORTUNE BRANDS	6789.6	13.7	77.7	4844.5x	3	-3.1	41.5	-77
31	472	FMC	2663.3	4.7	23.7	4259.0	8	0.6	-24.5	NM
INC	INC	TYCO INTERNATIONAL	27840.7	75.8	293.9	NA	NA	NA	NA	NA

16 METALS & MINING

INDUSTRY AVERAGE			3436.2	-13.4	-4.3	3781.7	5	8.6	159.5	12
1	224	ALUMINUM CO. OF AMERICA	12655.1	4.7	97.5	13319.2	2	9.8	805.1	56
2	225	USX-U.S. STEEL GROUP	3026.1	16.8	16.1	6871.0	5	3.9	452.0	64
3	278	NUCOR	4527.3	8.1	-6.5	4184.5	15	11.3	294.5	19
4	300	FREEPORT-McMORAN COPPER & GOLD	2913.2	-53.9	NA	2000.9	5	16.7	245.1	8
5	333	BETHLEHEM STEEL	1198.6	37.1	-32.5	4631.2	-1	-1.6	280.7	NM
6	359	ALCAN ALUMINUM	7057.5	-11.5	34.9	7777.0	2	-3.6	468.0	14
7	368	INLAND STEEL INDUSTRIES	1016.7	8.1	-25.8	5046.8	10	3.1	119.3	73
8	378	ARMCO	568.8	28.8	-19.8	1829.3	6	8.6	77.1	197
9	390	PHELPS DODGE	3721.1	-8.6	27.0	3914.3	3	4.3	408.5	-12
10	398	WORTHINGTON INDUSTRIES	1658.0	-17.4	-8.5	2043.8	17	13.5	93.3	-2
11	407	NEWMONT MINING	4537.7	-37.5	-17.2	1572.8	42	41.3	68.3	-31

INVESTMENT DATA								
RET. BEGIN 96	RETURN ON INVESTED CAPITAL	RETURN ON COMMON EQUITY	RECENT SHARE PRICE \$	12-MONTH HIGH/LOW \$	P-E RATIO	DIVIDEND YIELD	EARNINGS PER SHARE 1997	ESTIMATED EARNINGS PER SHARE 1998
2	15.4	20.0	47	51/27	16	1.29	2.85	3.04
6	21.5	24.9	39	39/25	23	0.98	1.69	1.91
3	14.6	23.8	56	61/42	14	1.57	3.90	4.32
7	16.0	20.9	60	63/40	26	0.80	2.33	2.62
9	12.5	18.9	45	49/28	24	1.71	1.86	2.17
5	10.8	17.4	65	73/50	13	0.31	5.11	5.65
3	11.2	16.7	48	48/28	21	1.26	2.31	2.92
6	30.6	35.8	85	106/80	17	2.58	5.06	4.27
9	9.7	17.7	46	46/32	25	1.57	1.82	2.09
8	13.9	16.6	32	42/26	12	2.23	2.69	2.84
3	8.2	12.7	56	56/35	22	1.66	2.48	3.66
8	10.4	17.0	31	31/18	15	1.56	2.01	2.26
3	14.1	34.6	41	65/32	22	1.77	1.85	1.83
5	14.4	16.9	43	46/35	17	1.98	2.44	2.75
2	16.1	51.8	84	84/44	26	0.69	3.28	3.88
1	8.2	19.3	35	49/31	12	1.13	3.01	3.33
1	13.2	19.8	58	59/33	17	1.52	3.51	4.42
2	6.2	15.6	130	135/44	17	0.60	7.55	7.50
2	6.7	12.7	50	51/30	21	0.95	2.35	2.62
0	11.3	15.8	58	83/48	11	1.90	5.48	6.20
1	43.8	45.0	24	30/21	16	3.75	1.46	1.57
6	0.1	0.1	39	40/18	-136	0.51	-0.29	1.95
5	11.8	13.6	29	31/23	31	2.21	0.95	1.18
8	12.8	18.7	44	54/43	22	2.53	2.04	3.24
0	7.1	8.6	56	58/43	17	2.36	3.34	4.04
6	-4.7	-6.9	48	49/36	-102	1.67	-0.47	2.40
8	17.3	33.7	27	45/23	20	3.27	1.32	1.74
9	0.9	1.0	40	56/30	27	2.12	1.48	1.70
1	-1.1	-2.6	72	91/59	-108	NA	-0.67	5.55
NA	NA	NA	51	53/27	NA	0.20	NA	1.89
9	5.8	7.7	27	37/23	17	1.85	1.61	1.63
9	10.6	17.5	73	90/65	16	1.36	4.62	5.80
2	18.3	26.7	35	41/25	7	2.85	4.88	4.14
8	13.2	16.3	52	63/44	15	0.78	3.35	3.56
9	6.9	21.6	15	34/13	14	1.33	1.06	0.60
6	14.6	20.2	11	13/8	5	NA	2.03	0.85
4	7.2	9.0	31	40/25	15	1.93	2.02	2.79
5	6.4	12.1	21	28/16	10	0.96	2.13	1.90
5	38.3	NM	5	6/3	10	NA	0.55	0.66
2	11.7	16.3	64	90/58	10	3.15	6.63	4.34
5	7.7	12.7	17	21/15	17	3.04	0.98	1.20
9	2.3	4.3	29	47/24	66	0.41	0.44	0.82



Metal Moves?

With its top performer, Aluminum Co. of America, reaching only the No. 224 berth on our list, no one would accuse the metals and mining group of red-hot growth. But there could be more activity in this sector in 1998. The combination of weak metal prices and U.S. companies waking up to the need for globalization should lead to overseas acquisitions and consolidation for the aluminum and steel makers. A good example: Alcoa's recent agreement to buy Alumat.

FOOTNOTES TO TABLES APPEAR ON PAGE 123;
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THE S&P Business Week's Industry Rankings

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MARKET VALUE

SALES

PROFITABILITY

			FEB. 27 1998 \$ MIL.	TOTAL RETURN (1 YEAR)	TOTAL RETURN 3 YEARS	12 MONTHS 1997 \$ MIL.	CHANGE FROM 1996 %	3 YEAR AVERAGE CHANGE %	12 MONTHS 1997 \$ MIL.	CHANGE FROM 1996 %
12	418	ASARCO	877.5	-24.8	-12.6	2721.0	0	7.4	143.4	4
13	428	REYNOLDS METALS	4605.5	1.5	33.6	6881.0	-1	4.5	136.0	31
14	429	ENGELHARD	2618.4	-15.6	8.4	3630.7y	14	14.7	66.5	-56
15	448	CYPRUS AMAX MINERALS	1530.6	-27.6	-32.8	3346.0	18	4.4	69.0	-10
16	485	PLACER DOME	3218.4	-39.0	-34.1	1209.0	4	10.6	-249.0	NM
17	488	BARRICK GOLD	7203.7	-30.5	-9.7	1284.0	-1	10.1	-123.0	NM
18	489	BATTLE MOUNTAIN GOLD	1378.8	-19.6	-35.8	344.9	-19	13.6	-5.1	NM
19	490	INCO	2944.4	-49.3	-31.5	2367.0	-4	-4.8	9.0	-94
20	496	HOMESTAKE MINING	1467.4	-38.3	-33.2	659.9y	-11	0.5	-168.9	NM

17 NonBANK FINANCIAL

INDUSTRY AVERAGE			16378.0	43.8	185.2	9394.0	13	15.2	869.8	23
1	10	MORGAN STANLEY, DEAN WITTER	41518.4	83.5	262.5	27132.0	22	19.5	2586.0	31
2	16	TRAVELERS GROUP	63696.2	57.8	346.4	37608.6	16	41.0	3103.7	5
3	19	MERRILL LYNCH	23784.1	53.3	265.5	31731.0	27	19.9	1906.0	18
4	25	CONSECO	8763.3	18.9	434.8	5568.4	82	41.4	574.2	106
5	26	MGIC INVESTMENT	8412.7	87.8	289.6	871.3	16	19.6	323.8	25
6	27	COUNTRYWIDE CREDIT INDUSTRIES	4799.0	52.7	183.8	2007.9	30	24.6	328.2	33
7	32	CHARLES SCHWAB	10018.2	47.3	289.5	2845.3	25	30.8	270.3	16
8	33	PROGRESSIVE	8366.2	76.4	201.7	4608.2y	32	23.3	400.0	28
9	34	SUNAMERICA	8876.3	46.1	415.1	1225.0y	43	16.8	422.3	46
10	36	LEHMAN BROTHERS HOLDINGS	7375.7	89.2	257.3	16883.0y	18	11.9e	647.0	56
11	42	FANNIE MAE	66900.3	55.9	253.5	27776.9y	11	14.2	3068.6	11
12	45	FREDDIE MAC	32150.1	53.0	240.5	14399.0	19	27.6	1395.0	11
13	49	ALLSTATE	40097.5	45.1	258.3	24949.0	3	5.8	3105.0	50
14	69	JEFFERSON-PILOT	5942.7	44.9	139.1	2578.3	21	27.5	394.4	34
15	86	WASHINGTON MUTUAL	17288.7	26.4	259.2	7446.5	7	83.6	481.8	109
16	93	AMERICAN INTERNATIONAL GROUP	84311.0	48.1	163.4	27916.5y	8	10.2	3332.3	15
17	112	AMERICAN EXPRESS	42005.4	41.5	182.3	17760.0y	8	4.4	1991.0	5
18	120	HOUSEHOLD INTERNATIONAL	13883.6	34.7	214.6	5453.1	8	5.0	686.6	27
19	123	MBIA	6539.8	53.7	148.1	654.0	20	14.5	374.2	16
20	133	ST. PAUL	7407.5	31.2	98.7	6219.3	8	9.4	773.2	39
21	145	CHUBB	14051.2	38.6	116.0	6664.0	17	4.1	769.5	58
22	150	GREEN TREE FINANCIAL	3095.4	-38.7	23.3	1707.7	34	39.0	301.4	63
23	152	CINCINNATI FINANCIAL	7411.4	100.1	182.8	1942.4	7	8.8	299.4	34
24	158	EQUIFAX	5161.4	36.9	172.2	1366.1	12	-4.0	185.5	21
25	165	BENEFICIAL	6262.4	74.8	253.1	2955.7	7	11.8	253.7	-10
26	169	AETNA	12983.8	5.2	74.4	18540.2y	22	15.1	901.1	339
27	170	MARSH & McLENNAN	14709.0	49.5	133.3	6008.6	36	20.1	399.4	-13
28	192	H.F. AHMANSON	5816.5	51.5	272.2	3649.9	-2	2.9	413.8	185
29	198	TORCHMARK	6546.4	61.7	139.2	2319.4	5	6.3	347.6	6
30	199	HARTFORD FINANCIAL SVCS. GROUP	11604.1	32.6	NA	13305.0	7	5.9	1332.0	NM
31	202	CIGNA	14164.4	27.6	173.2	20038.0y	6	2.6	1086.0	3
32	205	UNUM	7113.9	34.2	154.7	4004.1	-1	2.9	370.3	56

			INVESTMENT DATA					
NET GAIN 1996	RETURN ON INVESTED CAPITAL	RETURN ON COMMON EQUITY	RECENT SHARE PRICE \$	12-MONTH HIGH/LOW \$	P/E RATIO	DIVIDEND YIELD	EARNINGS PER SHARE 1997	ESTIMATED EARNINGS PER SHARE 1998
1.1	4.7	8.5	22	34/21	6	3.62	3.42	-1.29
1.5	3.2	5.0	62	80/54	34	2.25	1.84	4.92
1.7	5.3	7.6	18	24/17	39	2.21	0.46	1.22
1.7	1.1	2.1	16	27/14	30	4.89	0.54	0.33
1.6	-11.7	-16.1	13	21/11	-12	0.78	-1.06	0.23
1.8	-3.3	-3.8	19	28/15	-59	0.83	-0.33	0.75
1.5	-1.5	-2.6	6	8/4	-46	0.83	-0.13	-0.08
1.9	-0.3	-0.4	18	38/15	-177	0.57	-0.10	-0.07
1.1	-18.8	-31.8	10	17/8	-9	1.50	-1.15	-0.12
1.2	2.1	15.3	79	83/49	18	1.33	4.29	4.71
1.9	7.5	18.1	70	71/35	17	1.15	4.15	4.28
1.1	6.3	19.9	56	57/31	22	0.90	2.54	3.24
1.5	3.9	23.9	72	78/42	15	1.12	4.83	4.41
1.1	6.1	14.2	47	50/34	18	1.07	2.67	3.54
1.4	23.0	21.8	74	75/35	27	0.14	2.75	3.23
1.0	3.3	17.0	44	49/24	15	0.72	2.94	3.16
1.3	19.3	25.1	38	44/20	38	0.42	0.99	1.25
1.0	14.1	19.4	116	121/62	22	0.21	5.31	5.16
1.9	9.1	14.9	46	46/25	23	0.88	1.97	2.27
1.9	2.5	13.3	63	66/29	13	0.47	4.72	4.40
1.0	1.5	21.8	64	66/36	22	1.51	2.84	3.23
1.4	1.4	17.3	47	50/27	25	0.85	1.88	2.23
1.5	18.0	20.3	93	95/59	13	1.16	7.11	5.72
1.8	10.4	12.5	84	87/52	16	2.11	5.20	4.86
1.3	1.5	8.7	67	73/45	36	1.73	1.86	4.68
1.2	7.4	13.9	120	122/75	25	0.25	4.73	5.22
1.6	11.6	21.8	90	94/58	22	1.00	4.15	4.75
1.6	3.4	15.1	130	142/79	20	1.29	6.50	7.84
1.1	5.6	12.3	73	73/45	17	1.07	4.22	4.59
1.7	14.1	16.6	89	89/63	11	2.26	8.39	6.07
1.6	11.9	13.6	80	81/51	18	1.45	4.39	4.61
1.5	9.1	22.9	23	50/18	11	1.52	2.15	2.43
1.4	7.1	6.3	135	142/67	25	1.36	5.31	4.74
1.5	29.3	51.6	36	37/27	29	0.97	1.26	1.53
1.1	2.4	14.0	118	121/60	26	1.93	4.54	5.67
1.3	5.9	7.6	87	118/66	16	0.92	5.60	4.38
1.4	8.7	12.0	87	88/57	36	2.31	2.39	4.24
1.9	3.8	15.9	62	68/35	17	1.41	3.59	3.98
1.9	12.1	16.9	47	48/26	18	1.28	2.56	2.90
1.8	15.0	22.9	98	101/68	9	1.71	11.16	7.02
1.6	11.4	13.6	191	201/139	13	1.80	14.64	14.68
1.9	12.4	15.8	51	55/34	20	1.11	2.59	2.87



Dealer Wins

In a strong year for the dealmakers, some of the biggest deals involved their own stocks. Morgan Stanley Group combined with Dean Witter Discover, Travelers Group bought Salomon Brothers, and Merrill Lynch acquired Britain's Mercury Asset Management Group, pushing the merged firms to the top of the non-bank financial list. S&P newcomers Charles Schwab and Lehman Brothers also galloped into the top 50 with the help of bull market profits and takeover talk.

FOOTNOTES TO TABLES APPEAR ON PAGE 123.
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THE S&P 500 Business Week's Industry Rankings

			MARKET VALUE			SALES			PROFITABILITY	
			FEB. 27 1998 \$ MIL.	TOTAL RETURN (1 YEAR)	TOTAL RETURN (3 YEARS)	12 MONTHS 1997 \$ MIL.	CHANGE FROM 1996 %	3 YEAR AVERAGE CHANGE %	12 MONTHS 1997 \$ MIL.	CHANGE FROM 1996 %
33	206	AON	10031.2	43.5	180.7	5750.6	48	11.5	298.8	2
34	210	GOLDEN WEST FINANCIAL	5093.4	28.3	138.2	2878.4y	10	13.9	354.1	-4
35	236	GENERAL RE	16493.4	25.0	70.1	8246.6y	-1	27.6	967.7	8
36	241	SAFECO	6622.9	28.8	109.0	4770.3y	17	10.3	430.0	-2
37	268	TRANSAMERICA	7304.9	35.6	130.6	5726.5	8	0.6	532.0	6
38	284	AMERICAN GENERAL	14155.4	36.8	103.3	8927.0y	2	23.8	542.0	-17
39	310	H&R BLOCK	4940.8	63.9	37.3	1211.5	31	-7.3	131.1	14
40	318	LOEWS	11543.1	-1.1	112.8	20138.8y	-1	15.9	793.6	-43
41	400	DUN & BRADSTREET	5714.6	39.2	89.3	2154.4	0	0.1	311.0	NM
42	432	LINCOLN NATIONAL	8585.0	49.8	131.6	4898.5y	3	-9.8	22.2	-94
43	442	USF&G	2713.5	10.5	76.1	3404.0y	-3	1.2	194.0	-26

18 OFFICE EQUIPMENT & COMPUTERS

INDUSTRY AVERAGE			23310.8	41.1	211.3	8875.1	9	17.6	676.7	21
1	1	MICROSOFT	205264.5	76.3	438.1	13098.0	39	34.6	3895.0	57
2	2	DELL COMPUTER	45599.3	298.9	2596.4	12327.0	59	51.9	944.0	78
3	3	CISCO SYSTEMS	66679.6	79.5	485.6	7298.0	35	70.0	1323.1	27
4	5	COMPAQ COMPUTER	48703.7	103.0	364.9	24584.0	23	31.7	1855.0	41
5	8	EMC	18721.8	109.7	340.9	2937.9	29	27.6	538.5	39
6	9	COMPUTER ASSOCIATES INTL.	25800.9	59.5	180.3	4457.0	13	22.1	1103.0	274
7	20	SUN MICROSYSTEMS	17972.1	49.4	495.3	9206.6	18	20.1	718.6	27
8	23	HBO	10795.6	81.3	465.6	1203.2	27	31.9	143.5	74
9	37	PARAMETRIC TECHNOLOGY	7729.4	7.0	216.7	848.3	29	46.8	232.1	50
10	72	COMPUTER SCIENCES	8160.6	54.5	113.1	6266.9	17	26.0	256.0	96
11	74	INTERNATIONAL BUSINESS MACHINES	101531.6	47.3	186.1	78508.0	3	6.9	6093.0	12
12	92	HEWLETT-PACKARD	69749.8	18.9	139.7	44416.0	13	18.5	3136.0	16
13	102	ORACLE	24230.1	-7.7	76.6	6303.2	30	38.5	725.0	3
14	105	PITNEY BOWES	13296.4	53.7	186.0	4100.5	6	7.9	526.0	12
15	110	AUTOMATIC DATA PROCESSING	18253.4	44.6	104.2	4392.4y	12	19.1	545.4	13
16	121	XEROX	28964.5	45.9	156.8	18166.0	5	1.0	1452.0	20
17	129	ADOBE SYSTEMS	3038.6	26.7	27.0	911.9	16	13.9	186.8	22
18	141	SHARED MEDICAL SYSTEMS	1910.5	40.5	133.3	896.2y	15	17.8	60.4	23
19	288	CABLETRON SYSTEMS	2452.2	-47.0	-21.8	1446.4	9	24.8	196.6	27
20	328	DATA GENERAL	1002.1	8.6	161.9	1550.0	15	10.8	49.0	45
21	369	FIRST DATA	15187.8	-4.7	27.3	5234.5y	6	19.2	356.7	-44
22	383	BAY NETWORKS	7458.8	75.2	62.3	2302.1	10	23.8	-17.0	NM
23	406	DIGITAL EQUIPMENT	8357.9	70.6	69.3	13062.2	-4	-2.2	274.8	NM
24	419	UNISYS	3142.6	164.8	98.6	6636.0	4	3.2	-853.6	NM
25	424	AUTODESK	2209.4	36.7	23.3	632.4	24	8.9	15.4	-63
26	426	SILICON GRAPHICS	2828.0	-37.6	-56.5	3690.4	14	27.2	25.9	NM
27	452	SEAGATE TECHNOLOGY	5890.4	-51.9	102.6	8047.9	-6	14.0	-107.3	NM
28	456	CERIDIAN	3623.6	16.0	47.8	1074.8	14	-6.0	35.4	-74
29	473	DELUXE	2764.9	10.4	39.6	1919.4	-3	3.5	44.7	-32
30	477	MOORE	1384.9	-24.9	-1.7	2631.0	5	2.4	55.1	-63

INVESTMENT DATA								
NET RCIN 1996	RETURN ON INVESTED CAPITAL	RETURN ON COMMON EQUITY	RECENT SHARE PRICE \$	12 MONTH HIGH/LOW \$	P/E RATIO	DIVIDEND YIELD	EARNINGS PER SHARE 1997	ESTIMATED EARNINGS PER SHARE 1998
5.5	6.5	9.7	60	60/40	36	1.74	1.68	3.16
1.1	2.8	13.1	89	98/59	15	0.56	6.13	6.78
0.8	9.4	11.7	213	221/152	18	1.11	11.76	12.97
0.8	7.1	9.4	52	55/39	16	2.44	3.33	3.45
0.4	5.0	11.6	116	120/79	15	1.72	7.87	7.70
0.5	3.7	7.4	58	59/37	27	2.58	2.19	3.96
0.4	9.7	11.9	47	48/29	38	1.70	1.24	2.05
0.8	4.6	8.5	100	116/86	15	1.00	6.90	10.35
0.3	-264.7	NM	34	34/24	19	2.63	1.80	1.97
0.5	0.4	0.5	84	85/49	400	2.48	0.21	5.01
0.5	7.2	10.2	24	26/16	15	1.15	1.63	1.81
0.9	12.4	19.9	45	53/26	49	1.41	0.93	1.87
0.2	31.3	31.3	85	86/44	58	NA	1.47	1.65
0.8	72.1	73.0	70	72/15	55	NA	1.28	1.83
0.3	24.2	24.4	66	69/30	53	NA	1.25	1.74
0.6	19.7	19.7	32	40/14	27	0.19	1.19	1.69
0.0	19.9	24.6	38	39/16	36	NA	1.04	1.37
0.5	32.6	52.0	47	59/25	24	0.17	1.96	2.40
0.3	23.7	23.7	48	53/26	26	NA	1.84	2.31
0.7	15.9	15.9	54	56/21	81	0.15	0.67	1.27
0.4	32.0	32.0	30	32/19	35	NA	0.87	1.03
0.4	9.7	13.4	105	114/58	32	NA	3.25	3.94
0.1	18.2	30.7	104	114/64	17	0.77	6.01	6.81
0.9	16.5	19.1	67	73/48	23	0.84	2.94	3.36
0.5	24.4	27.2	25	42/18	34	NA	0.73	1.11
0.2	16.2	28.1	47	49/28	26	1.92	1.80	2.07
0.4	16.6	18.0	61	63/41	34	0.87	1.81	2.03
0.9	9.5	25.1	89	90/55	22	1.62	4.04	4.59
0.5	26.1	26.1	44	53/33	18	0.45	2.52	2.50
0.3	17.6	18.4	76	78/37	32	1.10	2.37	2.81
0.6	15.9	15.9	16	47/13	13	NA	1.24	1.03
0.5	6.6	9.3	21	38/13	19	NA	1.08	0.78
0.9	6.4	10.5	34	46/25	43	0.24	0.79	1.65
0.0	-1.1	-1.2	34	42/15	-261	NA	-0.13	1.09
0.5	5.8	7.0	57	63/25	36	NA	1.57	2.17
0.0	-26.9	-62.8	18	19/6	-3	NA	-5.30	0.90
0.2	4.5	4.5	47	51/29	153	0.51	0.31	2.09
0.9	1.1	1.4	15	30/11	108	NA	0.14	0.32
0.3	-2.9	-3.6	24	54/18	-50	NA	-0.49	-0.05
0.4	8.4	6.0	47	48/30	103	NA	0.45	1.86
0.3	6.3	7.4	34	37/30	62	4.35	0.55	2.37
0.0	4.4	4.6	16	23/14	27	5.99	0.59	0.66



Computer Clout

Turmoil in Asia, government investigations: Nothing has shaken the grip of the computer industry on the BW 50. Microsoft, Dell, and Cisco Systems squarely hold the top three slots in our elite rankings, and each moved up one notch from a year ago. Powering growth throughout the industry over the past year: computers that carry price tags of less than \$1,000, putting a PC within reach of almost everyone.

FOOTNOTES TO TABLES APPEAR ON PAGE 123.
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THE S&P 500 Business Week's Industry Rankings

			MARKET VALUE			SALES			PROFITABILITY		
			FEB. 27/ 1998 \$ MIL.	TOTAL RETURN (1 YEAR)	TOTAL RETURN (3 YEARS)	12 MONTHS 1997 \$ MIL.	CHANGE FROM 1996 %	3 YEAR AVERAGE CHANGE %	12 MONTHS 1997 \$ MIL.	CHANGE FROM 1996 %	3 YEAR AVERAGE CHANGE %
31	479	APPLE COMPUTER	3024.4	39.0	-39.5	6530.0	-26	-13.0	-878.0	NM	
32	481	JOHN H. HARLAND	471.0	-49.8	-26.0	562.7	-8	3.2	17.3	NM	
33	495	NOVELL	3690.5	-1.0	-48.3	884.5	-33	-24.9	-115.0	NM	
INC	INC	3COM	12675.6	2.1	37.2	5629.3	NA	NA	173.7	NA	

19 PAPER & FOREST PRODUCTS

INDUSTRY AVERAGE			7326.9	14.0	38.7	7324.7	0	4.3	70.2	-71	
1	214	KIMBERLY-CLARK	30661.8	5.5	135.7	12546.6	-5	17.1	884.0	-37	
2	394	FORT JAMES	9542.8	41.1	109.6	7259.0	-6	10.6	104.5	-68	
3	413	UNION CAMP	4164.6	26.5	28.5	4476.8	12	8.1	81.1	-5	
4	415	MEAD	3585.2	19.6	32.6	5077.4	8	2.3	150.1	-21	
5	445	WEYERHAEUSER	9965.4	10.2	35.8	11210.0	1	1.7	342.0	-26	
6	446	INTERNATIONAL PAPER	14094.7	11.4	30.9	20096.0	0	9.4	-151.0	NM	
7	450	WESTVACO	3312.7	14.8	34.6	2948.0	-3	1.1	159.7	-14	
8	455	BOISE CASCADE	1853.3	1.4	8.0	5493.8	8	8.9	-30.4	NM	
9	467	WILLAMETTE INDUSTRIES	4107.1	17.5	45.7	3438.7	0	2.8	73.0	-62	
10	470	GEORGIA-PACIFIC GROUP	5396.3	9.6	19.5	12968.0	1	-0.5	-86.0	NM	
11	478	POTLATCH	1253.9	3.7	12.9	1568.9	1	1.6	36.1	-41	
12	480	CHAMPION INTERNATIONAL	4908.6	15.2	25.8	5735.5	-2	0.6	-548.5	NM	
13	492	LOUISIANA-PACIFIC	2403.2	5.4	-16.5	2402.5	-3	-8.1	-101.8	NM	

20 PUBLISHING & BROADCASTING

INDUSTRY AVERAGE			12422.5	67.4	173.8	4250.5	18	15.4	51.8	-18	
1	47	CLEAR CHANNEL COMMUNICATIONS	8875.2	87.6	536.5	697.1	98	57.1	63.6	69	
2	77	TRIBUNE	7937.1	64.7	142.5	2719.8	13	8.0	393.6	39	
3	90	KNIGHT-RIDDER	4829.9	43.2	117.8	2876.8	21	1.0	396.5	114	
4	99	GANNETT	18315.0	62.7	149.1	4729.5	7	8.4	712.7	14	
5	116	MEREDITH	2269.7	77.3	264.6	926.0	9	4.3	75.5	29	
6	147	NEW YORK TIMES	6280.5	50.7	221.0	2866.4	9	7.0	262.3	210	
7	167	MCGRAW-HILL	7486.9	50.9	133.7	3534.1	15	8.2	290.7	-41	
8	239	TIMES MIRROR	5448.0	19.6	241.0	3318.5	-2	-0.5	250.3	21	
9	240	TIME WARNER	38913.8	65.9	79.3	13294.0	32	21.9	301.0	NM	
10	303	COMCAST	12214.5	98.0	125.5	4912.6	22	49.2	-208.5	NM	
11	376	TELE-COMMUNICATIONS	14851.9	133.7	86.1	6653.0a	17	5.7	-399.0a	NM	
12	381	CBS	22005.0	83.6	105.8	5363.0	29	-5.6	-131.0	NM	
13	386	U S WEST MEDIA GROUP	19539.8	76.4	NA	5043.0	10	42.9	-480.0	NM	
14	465	DOW JONES	4947.8	29.2	56.2	2572.5	4	7.3	-802.1	NM	

21 SERVICE INDUSTRIES

INDUSTRY AVERAGE			6713.6	27.3	84.2	5519.9	17	15.9	90.6	-53	
1	30	OMNICOM GROUP	7412.5	84.6	262.4	3124.8	18	17.8	222.4	26	
2	57	INTERPUBLIC GROUP	6878.4	65.1	150.0	3125.8y	23	18.1	239.1	17	
3	78	SERVICE CORP. INTERNATIONAL	9538.3	30.6	177.5	2468.4	8	31.1	374.6	41	

INVESTMENT DATA								
NET GAIN 1996	RETURN ON INVESTED CAPITAL	RETURN ON COMMON EQUITY	RECENT SHARE PRICE \$	12 MONTH HIGH/LOW \$	P-E RATIO	DIVIDEND YIELD	EARNINGS PER SHARE 1997	ESTIMATED EARNINGS PER SHARE 1998
9.8	-40.0	-70.6	24	30/13	-3	NA	-7.01	1.08
2.3	5.7	8.9	15	31/14	27	1.98	0.56	1.18
3.6	-7.2	-7.3	11	11/6	-32	NA	-0.33	0.18
NA	6.9	7.0	36	60/24	74	NA	0.48	1.89
4.4	1.3	2.2	44	55/35	NM	2.17	0.03	1.98
0.7	14.3	20.7	56	57/43	35	1.80	1.58	2.85
4.3	1.3	10.5	46	47/27	131	1.31	0.35	2.68
2.1	2.5	3.9	60	65/45	51	3.01	1.17	2.61
4.0	4.0	6.6	34	38/25	24	1.87	1.41	1.96
4.2	3.7	7.4	50	64/43	29	3.20	1.71	2.60
5.5	-0.9	-1.7	47	61/39	-93	2.15	-0.50	2.17
5.1	4.2	7.1	33	38/25	21	2.71	1.57	1.98
0.2	-1.8	-3.9	33	46/28	-28	1.81	-1.19	0.89
6.6	1.9	3.7	37	44/29	56	1.73	0.66	1.56
0.3	-1.1	-2.4	59	109/52	-62	1.70	-0.94	2.01
4.0	2.2	3.8	43	53/39	35	4.02	1.25	1.81
2.4	-8.6	-17.1	51	67/42	-9	0.39	-5.72	2.11
3.1	-5.5	-7.9	22	26/17	-23	2.55	-0.94	0.45
4.8	2.9	0.5	55	56/32	93	1.08	0.59	1.36
0.7	2.4	3.7	91	93/42	135	NA	0.67	0.61
4.8	11.2	21.2	65	65/39	23	1.05	2.81	2.58
7.8	11.6	23.4	56	57/36	14	1.42	3.91	2.55
4.1	14.6	21.7	65	65/39	26	1.18	2.50	2.82
5.9	12.7	21.7	43	44/22	32	0.65	1.36	1.41
3.2	11.5	16.0	65	68/40	25	1.04	2.66	2.89
5.1	14.7	20.6	76	78/49	26	2.06	2.91	†
5.1	12.1	25.2	62	63/49	27	1.17	2.29	2.75
6.6	-0.1	-0.2	68	70/40	NM	0.53	-0.03	-0.13
4.3	-2.7	-13.3	35	36/15	-53	0.27	-0.66	-0.49
6.0	-2.6	-995.5	29	31/11	-45	NA	-0.65	-0.20
5.3	-1.2	-2.2	31	33/16	-129	0.65	-0.24	0.30
4.2	-3.2	-7.4	32	33/16	-37	NA	-0.88	-0.87
7.7	-40.0	-47.7	51	56/38	-6	1.87	-8.36	1.48
4.1	9.3	5.4	43	47/29	35	1.69	1.20	2.17
5.7	15.1	27.1	46	47/24	33	1.09	1.37	1.59
3.1	15.8	26.2	55	56/33	29	0.95	1.90	2.19
4.6	7.6	14.3	38	40/28	26	0.95	1.47	1.54



Now Hear This

Clear Channel Communications has a message. And if it can't reach you on one of its 184 radio stations or 18 TV stations, just look to the side of the road. This Texas media company is now the biggest billboard owner in the land. New to the S&P 500, it managed to nearly double sales last year and leap to the top of its industry group thanks to \$3.5 billion in acquisitions, including the \$1.7 billion purchase of billboard giant Universal Outdoor. Those buys also let it offer advertisers all three media in some markets—a clear advantage.

FOOTNOTES TO TABLES APPEAR ON PAGE 123;
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THE S&P 500

Business Week's Industry Rankings

			MARKET VALUE			SALES			PROFITABILITY	
			FEB. 27 1998 \$ MIL.	TOTAL RETURN (1 YEAR)	TOTAL RETURN (3 YEARS)	12 MONTHS 1997 \$ MIL.	CHANGE FROM 1996 %	3 YEAR AVERAGE CHANGE %	12 MONTHS 1997 \$ MIL.	CHANGE FROM 1996 %
4	148	CRANE	2248.1	51.0	157.2	2036.8	10	6.8	112.8	22
5	182	COGNIZANT	8094.9	44.2	NA	1418.2	9	2.0	312.4	25
6	217	W.W. GRAINGER	4810.3	23.1	64.4	4136.6	17	10.7	231.8	11
7	251	CENDANT	16003.3	54.6	139.4	5314.7	36	75.0	55.4	-87
8	313	GENUINE PARTS	6611.7	20.7	56.4	6005.2	5	7.5	342.4	4
9	314	SAFETY-KLEEN	1565.9	49.7	73.1	1007.9	9	8.3	63.2	3
10	329	ENRON	14051.2	20.6	52.4	20273.0	53	32.5	105.0	-82
11	380	FLUOR	3957.1	-21.9	0.7	14263.5	18	19.5	139.0	-49
12	417	BROWNING-FERRIS INDUSTRIES	6500.8	8.0	14.9	5632.6	-4	5.6	298.6	NM
13	433	R.R. DONNELLEY	5780.0	29.3	22.5	4850.0	-4	-2.8	206.5	NM
14	444	EG&G	1219.0	29.4	104.1	1460.8	2	2.9	30.6	-44
15	468	FOSTER WHEELER	1089.6	-31.8	-13.0	4011.0	0	22.5	-10.5	NM
16	483	WASTE MANAGEMENT	11656.0	-20.8	0.8	9188.6	0	-2.6	-1274.2	NM

22 TELECOMMUNICATIONS

INDUSTRY AVERAGE			36910.6	40.9	118.9	15232.4	8	16.7	1220.7	-7
1	7	TELLABS	10956.6	56.8	364.4	1203.5	39	34.8	263.7	124
2	31	NORTHERN TELECOM	27717.7	49.4	220.6	15449.0y	20	20.3	829.0	33
3	55	AIRTOUCH COMMUNICATIONS	22639.4	66.2	65.4	3594.0	60	42.4	448.0	125
4	81	BELLSOUTH	60450.5	36.0	129.4	20561.0	8	6.8	3270.0	14
5	89	AMERITECH	45610.3	36.8	117.7	15998.0	7	8.6	2296.0	8
6	132	BELL ATLANTIC	69703.3	35.7	90.7	30193.9	4	36.7	2454.9	-22
7	174	GTE	51851.8	20.9	85.8	23260.0	9	6.1	2794.0	0
8	180	WORLDCom	34642.6	38.9	225.9	7351.4	64	46.2	383.7	NM
9	183	ALLTEL	8391.7	35.1	76.3	3263.6	2	3.6	507.9	74
10	185	U S WEST COMMUNICATIONS GROUP	25224.5	53.2	157.5	10319.0	2	4.2	1180.0	-3
11	215	SBC COMMUNICATIONS	69317.0	38.1	99.8	24856.0	6	33.6	1474.0	-54
12	226	SPRINT	28380.0	50.8	192.7	14873.9	7	7.6	952.5	-20
13	253	AT&T	99142.4	56.9	91.9	51319.0	2	-10.8	4472.0	-20
14	322	LUCENT TECHNOLOGIES	70371.9	100.6	NA	27146.0	14	12.6e	474.0	-56
15	351	MCI COMMUNICATIONS	31747.8	34.8	138.8	19653.0	6	14.5	2.0	-100
16	373	SCIENTIFIC-ATLANTA	1384.0	-0.4	-24.4	1213.4	11	7.0	67.4	220
17	434	DSC COMMUNICATIONS	2314.1	-4.3	-45.5	1575.5	14	14.2	48.9	NM
18	449	FRONTIER	4545.0	31.3	34.7	2352.9	-9	12.9	54.6	-75

23 TRANSPORTATION

INDUSTRY AVERAGE			9136.7	45.5	166.8	9097.3	9	8.8	623.7	25
1	14	US AIRWAYS GROUP	5769.0	216.6	977.7	8513.8	5	7.0	1024.7	289
2	68	SOUTHWEST AIRLINES	6287.4	81.5	145.5	3816.8	12	14.2	317.8	53
3	83	DELTA AIR LINES	8425.3	41.6	96.5	13946.0	8	5.0	934.0	275
4	157	FDX	7335.2	25.2	95.6	12571.4	16	11.9	445.8	45
5	176	AMR	11538.9	58.5	107.1	18570.0	5	4.8	985.0	-11
6	19	BURLINGTON NORTHERN SANTA FE	15607.3	20.8	86.2	8413.0	3	20.2	885.0	0
7	332	NORFOLK SOUTHERN	12984.6	19.3	68.1	4223.0y	3	-3.7	806.0	7
8	347	UNION PACIFIC	12637.9	-11.5	52.0	11079.0	26	19.3	432.0	-41

RANK	RETURN ON INVESTED CAPITAL	RETURN ON COMMON EQUITY	INVESTMENT DATA					
			RECENT SHARE PRICE \$	12-MONTH HIGH/LOW \$	P-E RATIO	DIVIDEND YIELD	EARNINGS PER SHARE 1997	ESTIMATED EARNINGS PER SHARE 1998
0	14.2	21.2	49	50/31	20	1.02	2.44	2.83
1	34.6	39.0	50	50/28	27	0.24	1.86	2.13
9	17.5	17.5	97	100/71	21	1.12	4.54	5.13
8	2.4	3.4	38	39/19	625	NA	0.06	NA
8	17.2	19.1	37	37/30	19	2.70	1.90	2.11
6	8.5	12.7	27	29/14	25	1.34	1.07	1.23
4	0.6	1.7	47	48/35	147	2.02	0.32	2.31
3	6.8	8.0	47	65/34	27	1.69	1.73	2.52
7	6.9	14.7	33	39/26	22	2.28	1.49	1.96
4	6.9	12.5	40	42/30	28	2.02	1.42	1.91
8	7.1	9.7	27	28/18	40	2.08	0.67	1.26
1	-0.7	-1.7	27	48/22	-103	3.14	-0.26	2.20
4	-10.8	-30.5	25	35/22	-9	2.72	-2.73	1.66

3	10.0	16.3	54	57/32	33	2.10	1.64	2.30
6	28.2	28.3	60	65/32	43	NA	1.42	1.73
8	12.3	16.5	53	57/31	34	0.56	1.56	1.90
8	5.5	7.1	45	46/22	58	NA	0.78	1.02
0	14.5	21.6	61	63/39	19	2.36	3.29	3.10
3	17.8	27.6	42	46/28	20	2.88	2.08	2.33
7	9.2	19.6	90	94/57	29	3.43	3.13	5.47
1	11.5	36.2	54	56/41	19	3.47	2.90	3.09
8	1.9	2.7	38	40/21	95	NA	0.40	0.86
1	12.4	22.9	46	47/30	17	2.54	2.70	2.28
1	12.8	28.1	52	55/31	21	4.11	2.44	2.75
6	6.6	15.5	76	79/49	47	2.47	1.60	4.18
6	7.4	10.5	66	68/42	30	1.52	2.18	1.88
0	15.4	20.3	61	67/31	22	2.16	2.74	3.20
6	7.2	10.1	108	111/49	155	0.28	0.70	3.05
5	0.0	0.0	48	48/27	NC	0.11	0.00	1.11
9	11.6	11.6	18	25/14	20	0.34	0.86	0.86
5	2.6	4.0	20	33/17	48	NA	0.41	1.30
5	2.9	5.2	28	28/15	84	3.21	0.33	1.23

0	10.0	14.8	63	71/43	13	1.51	4.85	5.25
2	31.4	155.0	63	73/20	6	NA	9.87	5.20
1	12.5	16.7	29	32/14	20	0.14	1.40	1.70
9	17.5	25.8	113	125/80	9	0.18	12.04	12.99
8	9.9	13.9	64	85/50	17	NA	3.81	4.78
2	9.7	16.4	127	137/79	12	NA	10.78	12.18
9	7.4	13.0	100	102/70	18	1.21	5.64	7.24
4	6.3	15.2	34	38/28	16	2.32	2.19	2.20
3	2.6	5.1	51	73/49	29	1.57	1.74	3.81



Plane Genius

At No. 14 in the BW 50, highflying US Airways Group shows the power of a decisive turnaround. Just three years ago, the carrier was mired in losses, but under a new CEO, it has gained altitude. Stephen M. Wolf, who joined the airline two years ago, won labor concessions, created the low-cost, short-haul carrier MetroJet, and is bringing order to US Airways' fleet and facilities. The result: It ranked No. 2 among all the S&P 500 companies for three-year earnings growth and total returns.

FOOTNOTES TO TABLES APPEAR ON PAGE 123; ALPHABETICAL INDEX OF COMPANIES BEGINS ON PAGE 150

THE S&P 500

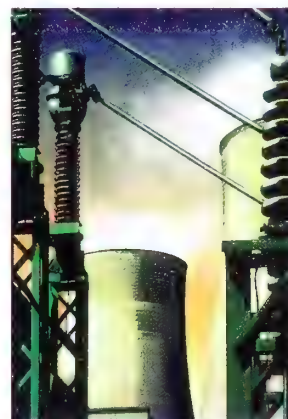
Business Week's Industry Rankings

			MARKET VALUE			SALES			PROFITABILITY	
			FEB. 1998 \$ MIL.	TOTAL RETURN (1 YEAR)	TOTAL RETURN (3 YEARS)	12 MONTHS 1997 \$ MIL.	CHANGE FROM 1996 %	3 YEAR AVERAGE CHANGE %	12 MONTHS 1997 \$ MIL.	CHANGE FROM 1996 %
9	352	CSX	12211.8	21.8	53.6	10621.0	1	3.3	799.0	-7
10	377	LAIDLAW	4841.4	8.0	84.8	3422.0	44	14.1	71.3	-47
11	420	RYDER SYSTEM	2865.1	18.6	68.1	4893.9	-1	0.9	160.2	NM

24 UTILITIES

INDUSTRY AVERAGE			6569.0	23.7	68.3	5621.7	21	12.3	388.1	-12
1	85	WILLIAMS	10448.3	57.5	271.3	4409.6	25	34.8	350.5	-3
2	114	COLUMBIA ENERGY GROUP	4235.0	32.5	201.0	5053.6y	51	23.0	273.3	23
3	153	DUKE ENERGY	19997.1	31.0	62.3	16308.9y	33	62.2	974.4	-9
4	163	CONSOLIDATED NATURAL GAS	5489.1	17.1	75.6	5710.0y	50	22.5	304.4	2
5	231	CINERGY	5491.6	6.8	65.7	4352.8	34	13.8	375.2	5
6	250	HOUSTON INDUSTRIES	7305.7	19.8	66.2	6873.4y	68	21.1	423.4	-1
7	254	PG&E	12671.8	38.9	43.1	15399.9y	60	12.6	749.1	-1
8	263	SOUTHERN	17024.6	20.3	41.8	12680.0	22	14.9	1025.3	-15
9	276	FPL GROUP	10562.0	34.6	83.5	6369.0y	6	5.7	637.6	6
10	281	FIRSTENERGY	4415.0	37.9	69.4	2823.9	14	5.4	341.1	3
11	296	NICOR	1988.3	28.0	89.0	1992.6y	8	9.0	127.9	6
12	298	EDISON INTERNATIONAL	10689.6	32.3	97.1	9235.1y	8	3.3	742.5	-3
13	299	CONSOLIDATED EDISON	9988.9	47.6	89.4	7121.3	2	4.0	712.8	3
14	301	TEXAS UTILITIES	9614.4	7.1	48.9	7945.6	21	12.4	687.4	-15
15	305	SONAT	3697.9	-4.4	61.4	4174.6	37	36.0	175.9	-13
16	321	AMERICAN ELECTRIC POWER	9101.3	22.5	69.7	6161.3	5	3.8	638.2	1
17	325	GPU	4865.9	23.2	58.4	4143.4	4	4.3	347.5	14
18	326	DOMINION RESOURCES	7448.4	7.8	28.6	7436.3y	54	16.8	434.7	-14
19	327	AMEREN	3925.4	7.0	23.2	3326.5	0	20.2	399.1	7
20	331	DTE ENERGY	5332.4	28.6	57.0	3764.5	3	2.1	429.0	32
21	335	ENTERGY	7035.5	19.2	59.3	9561.7y	33	16.8	300.9	-39
22	337	PACIFICORP	7172.7	22.5	47.9	6278.0y	65	20.4	225.4	-48
23	339	ONEOK	1093.9	27.3	131.6	1227.3y	-1	16.7	59.6	5
24	360	CENTRAL & SOUTH WEST	5690.7	19.3	33.9	5268.0y	2	17.6	331.0	5
25	362	CAROLINA POWER & LIGHT	6276.7	20.0	77.7	3024.1	1	1.5	388.3	-1
26	370	PUBLIC SERVICE ENTERPRISE GROUP	7480.6	24.1	39.7	6370.0y	5	2.5	574.0	-3
27	389	PACIFIC ENTERPRISES	3028.1	24.6	72.0	2738.0y	7	1.7	191.0	-9
28	395	BALTIMORE GAS & ELECTRIC	4660.8	23.1	53.4	3307.6y	5	6.1	282.8	-9
29	401	PP&L RESOURCES	3711.4	6.8	35.1	3048.7y	5	4.0	319.3	-11
30	405	PEOPLES ENERGY	1270.2	11.0	63.3	1272.4	0	3.6	96.5	-8
31	414	NORTHERN STATES POWER	4099.4	23.1	44.3	2733.8	3	3.2	237.3	-14
32	416	EASTERN ENTERPRISES	903.0	38.5	92.3	970.2	-4	2.0	52.0	-14
33	418	PECO ENERGY	4409.2	-1.9	-8.8	4618.0	8	4.3	337.0	-35
34	425	NIAGARA MOHAWK POWER	1850.4	19.2	-6.7	3977.2a	0	0.0	217.0a	32
35	441	UNICOM	6938.8	56.9	51.9	7083.0	2	3.7	-178.8	NM

RANK	FIRM	MARKET CAPITALIZATION	RETURN ON INVESTED CAPITAL	RETURN ON COMMON EQUITY	INVESTMENT DATA					
					RECENT SHARE PRICE \$	12-MONTH HIGH/LOW \$	P-E RATIO	DIVIDEND YIELD	ESTIMATED EARNINGS PER SHARE 1997	ESTIMATED EARNINGS PER SHARE 1998
1	1	1	6.6	13.9	56	62/44	15	2.15	3.62	4.24
2	2	2	1.2	2.5	15	17/13	70	1.07	0.21	0.81
3	3	3	5.1	13.5	37	39/29	18	1.64	2.05	2.64
4	4	4								
5	5	5	5.2	9.1	37	40/28	17	4.74	2.19	2.61
6	6	6	4.4	9.7	33	35/19	32	1.83	1.04	1.24
7	7	7	7.2	15.3	76	79/56	16	1.31	4.90	5.33
8	8	8	6.3	10.9	56	57/42	22	3.96	2.51	3.43
9	9	9	8.2	13.2	58	61/47	18	3.37	3.15	3.60
10	10	10	7.6	13.6	35	39/32	15	5.17	2.28	2.61
11	11	11	3.9	8.4	26	27/19	16	5.80	1.66	1.88
12	12	12	4.0	7.5	30	31/22	17	3.98	1.75	1.80
13	13	13	4.3	9.5	25	26/20	17	5.43	1.42	1.78
14	14	14	7.6	12.2	58	60/43	16	3.45	3.57	3.74
15	15	15	5.7	10.8	29	30/19	15	5.18	1.94	2.28
16	16	16	9.9	17.4	41	43/30	16	3.40	2.61	2.67
17	17	17	5.2	11.0	28	28/19	16	3.77	1.73	1.82
18	18	18	6.6	11.1	43	44/27	14	4.99	2.95	2.95
19	19	19	3.9	9.5	40	43/32	14	5.44	2.85	3.23
20	20	20	6.4	11.0	43	59/39	21	2.50	2.01	2.38
21	21	21	6.2	12.9	48	52/39	15	5.00	3.28	3.41
22	22	22	4.9	10.1	40	43/31	15	4.98	2.77	3.35
23	23	23	2.9	7.0	40	43/33	19	6.47	2.15	3.12
24	24	24	8.8	15.0	38	44/35	14	6.61	2.82	2.84
25	25	25	5.4	11.4	37	38/26	13	5.61	2.88	2.87
26	26	26	1.4	3.3	29	30/22	28	6.22	1.03	2.59
27	27	27	2.1	4.4	24	27/19	36	4.47	0.68	1.73
28	28	28	4.1	5.3	35	41/26	16	3.43	2.13	2.26
29	29	29	4.1	8.6	27	28/18	17	6.49	1.55	1.92
30	30	30	7.2	13.3	42	43/33	16	4.65	2.66	2.94
31	31	31	5.3	10.4	32	33/23	13	6.70	2.41	2.74
32	32	32	7.0	11.6	36	38/30	16	4.19	2.21	2.31
33	33	33	4.1	8.0	32	34/25	18	5.20	1.72	2.39
34	34	34	5.2	10.3	22	24/19	12	7.46	1.80	2.04
35	35	35	7.6	13.1	36	40/31	13	5.32	2.75	2.62
36	36	36	4.8	8.8	55	59/45	17	5.13	3.21	3.92
37	37	37	6.1	11.6	44	46/31	17	3.70	2.54	2.77
38	38	38	4.4	10.8	20	25/19	14	5.05	1.44	2.13
39	39	39	2.7	5.5	13	13/8	10	NA	1.25	0.37
40	40	40	-2.0	-4.3	32	32/19	-29	4.99	-1.10	2.45



In the Pipeline

How do you grow if you're stuck in a low-margin, highly regulated business? That's the problem facing much of the utilities industry, which failed to place any company in the BW 50 this year. Deregulation has thrown some markets up for grabs, so many companies are branching out into new areas. Group leader Williams, at No. 85 overall, is investing cash flow from low-margin gas pipeline operations into unregulated energy and telecom businesses.

FOOTNOTES TO TABLES APPEAR ON PAGE 123;
ALPHABETICAL INDEX OF COMPANIES
BEGINS ON PAGE 150

THE S&P 500

Alphabetical List of Companies

The number to the left of the company's name identifies its overall rank among Business Week's Performance Rankings of the S&P 500 companies. That list begins on page 91. The numbers immediately to the right identify the company's rank in market value and 12-month sales and profits, respectively, among the 500.

RANK	COMPANY (INDUSTRY GROUP)	OTHER RANKINGS			RANK	COMPANY (INDUSTRY GROUP)	OTHER RANKINGS		
		MARKET VALUE	SALES	PROFITS			MARKET VALUE	SALES	PROFITS
A									
96	ABBOTT LABORATORIES (12)	32	112	39	418	ASARCO (16)	497	359	355
129	ADOBE SYSTEMS (18)	401	479	325	221	ASHLAND (11)	352	91	304
474	ADVANCED MICRO DEVICES (9)	385	379	461	253	AT&T (22)	15	11	10
269	AEROQUIP-VICKERS (15)	466	396	389	171	ATLANTIC RICHFIELD (11)	79	62	45
169	AETNA (17)	148	64	90	424	AUTODESK (18)	442	493	450
192	AHMANSON (H.F.) (17)	295	310	179	110	AUTOMATIC DATA PROCESSING (18)	105	274	139
173	AIR PRODUCTS & CHEMICALS (4)	195	259	150	196	AUTOZONE (8)	338	356	317
55	AIRTOUCH COMMUNICATIONS (22)	87	315	164	193	AVERY DENNISON (7)	313	325	315
306	ALBERTO-CULVER (6)	459	424	401	208	AVON PRODUCTS (6)	204	242	223
B									
265	ALBERTSON'S (10)	171	81	147	317	BAKER HUGHES (11)	265	297	360
359	ALCAN ALUMINUM (16)	260	170	155	397	BALL (7)	493	377	423
224	ALCOA (16)	155	92	100	395	BALTIMORE G&E (24)	335	329	268
233	ALLEGHENY TELEDYNE (5)	333	306	260	156	BANC ONE (3)	56	128	61
361	ALLERGAN (12)	436	470	371	113	BANK OF NEW YORK (3)	91	241	73
188	ALLIEDSIGNAL (5)	84	83	69	94	BANKAMERICA (3)	36	47	22
49	ALLSTATE (17)	51	36	25	73	BANKBOSTON (3)	131	218	93
183	ALLTEL (22)	223	331	148	142	BANKERS TRUST (3)	172	150	95
437	ALZA (12)	391	497	485	427	BARD (C.R.) (12)	452	459	406
461	AMERADA HESS (11)	308	160	453	488	BARRICK GOLD (16)	257	452	475
327	AMEREN (24)	364	326	188	489	BATTLE MOUNTAIN GOLD (16)	474	498	456
321	AMERICAN ELECTRIC (24)	208	211	127	438	BAUSCH & LOMB (12)	423	413	437
112	AMERICAN EXPRESS (17)	47	66	41	319	BAXTER INTERNATIONAL (12)	121	212	255
284	AMERICAN GENERAL (17)	134	149	140	383	BAY NETWORKS (18)	244	382	459
257	AMERICAN GREETINGS (14)	387	388	323	71	BB&T (3)	227	384	211
88	AMERICAN HOME (12)	28	66	40	260	BECTON, DICKINSON (12)	237	353	248
93	AMERICAN INTL. GROUP (17)	16	28	17	132	BELL ATLANTIC (22)	21	25	34
385	AMERICAN STORES (10)	268	58	270	81	BELLSOUTH (22)	30	49	20
89	AMERITECH (22)	45	71	36	290	BEMIS (7)	431	416	383
227	AMGEN (12)	140	375	126	165	BENEFICIAL (17)	288	344	283
286	AMOCO (11)	49	21	31	308	BESTFOODS (10)	127	159	175
280	AMP (9)	197	221	158	333	BETHLEHEM STEEL (16)	480	264	269
176	AMR (23)	170	63	81	130	BIOMET (12)	386	494	376
237	ANADARKO PETROLEUM (11)	367	490	385	274	BLACK & DECKER (15)	331	249	300
249	ANDREW (9)	426	482	381	310	BLOCK (H&R) (17)	321	461	365
293	ANHEUSER-BUSCH (6)	86	120	68	316	BOEING (1)	38	13	481
206	AON (17)	189	220	257	455	BOISE CASCADE (19)	455	229	463
194	APACHE (11)	400	466	347	65	BOSTON SCIENTIFIC (12)	166	418	229
479	APPLE COMPUTER (18)	404	199	496	436	BRIGGS & STRATTON (15)	485	447	425
13	APPLIED MATERIALS (15)	144	268	118	22	BRISTOL-MYERS SQUIBB (12)	14	69	23
365	ARCHER DANIELS MIDLAND (10)	150	79	161	287	BROWN-FORMAN (6)	368	431	332
378	ARMCO (16)	498	420	402	417	BROWNING-FERRIS (21)	281	225	259
289	ARMSTRONG WORLD (6)	394	389	328	348	BRUNSWICK (14)	396	309	349

Why Are So Many Investors Choosing Prudential For Their Retirement Planning?

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The number to the left of the company's name identifies its overall rank among Business Week's Performance Rankings. For an explanation of other rankings, see page 150.

RANK	COMPANY (INDUSTRY GROUP)	OTHER RANKINGS			RANK	COMPANY (INDUSTRY GROUP)	OTHER RANKINGS		
		MARKET VALUE	SALES	PROFITS			MARKET VALUE	SALES	PROFITS
195	BURLINGTON NORTHERN SANTA FE (23)	123	158	91	291	COOPER INDUSTRIES (9)	267	236	190
334	BURLINGTON RESOURCES (11)	233	405	240	356	COOPER TIRE & RUBBER (2)	457	423	374
C					292	COORS (ADOLPH) (6)	482	421	397
					39	CORESTATES FINANCIAL (3)	116	295	104
288	CABLETRON SYSTEMS (18)	425	439	318	230	CORNING (15)	203	288	169
131	CAMPBELL SOUP (10)	75	163	88	62	COSTCO (8)	184	46	201
87	CARDINAL HEALTH (12)	211	115	302	27	COUNTRYWIDE CREDIT (17)	329	403	232
362	CAROLINA POWER (24)	286	341	196	148	CRANE (21)	440	399	380
126	CASE (15)	324	214	184	315	CROWN CORK & SEAL (7)	266	157	251
57	CATERPILLAR (15)	98	59	48	352	CSX (23)	164	125	102
381	CBS (20)	90	232	477	342	CUMMINS ENGINE (15)	443	227	312
251	CENDANT (21)	120	235	428	283	CVS (12)	151	101	442
201	CENTEX (13)	445	303	368	448	CYPRUS AMAX MINERALS (16)	469	324	410
360	CENTRAL & SOUTH WEST (24)	302	237	230	D				
456	CERIDIAN (18)	377	472	444					
480	CHAMPION INTL. (19)	323	222	492	104	DANA (2)	299	153	209
486	CHARMING SHOPPES (8)	499	474	448	469	DARDEN RESTAURANTS (14)	450	335	469
24	CHASE MANHATTAN (3)	39	31	13	328	DATA GENERAL (18)	491	437	438
160	CHEVRON (11)	37	19	21	53	DAYTON HUDSON (8)	115	30	101
312	CHRYSLER (2)	78	9	29	80	DEERE (15)	139	95	80
145	CHUBB (17)	137	194	109	2	DELL COMPUTER (18)	46	110	86
202	CIGNA (17)	132	54	75	83	DELTA AIR LINES (23)	221	87	87
152	CINCINNATI FINANCIAL (17)	248	410	256	473	DELUXE (18)	413	411	440
219	CINCINNATI MILACRON (15)	478	415	400	406	DIGITAL EQUIPMENT (18)	225	99	271
231	CINERGY (24)	304	277	202	374	DILLARD'S (8)	362	197	281
357	CIRCUIT CITY STORES (6)	370	171	373	91	DISNEY (WALT) (14)	17	45	42
3	CISCO SYSTEMS (18)	26	180	60	326	DOMINION RESOURCES (24)	246	176	171
245	CITICORP (3)	31	24	15	433	DONNELLEY (R.R.) (21)	296	254	314
47	CLEAR CHANNEL COMMUNS. (20)	213	487	417	75	DOVER (15)	218	267	183
106	CLOROX (6)	209	363	276	282	DOW CHEMICAL (4)	95	55	47
340	COASTAL (11)	274	136	193	465	DOW JONES (20)	320	368	494
119	COCA-COLA (6)	3	60	11	118	DRESSER INDUSTRIES (15)	236	174	233
182	COGNIZANT (21)	229	442	244	434	DSC COMMUNICATIONS (22)	435	434	439
97	COLGATE-PALMOLIVE (6)	82	148	112	331	DTE ENERGY (24)	312	304	174
114	COLUMBIA ENERGY GROUP (24)	351	244	272	153	DUKE ENERGY (24)	100	70	82
457	COLUMBIA/HCA HEALTHCARE (12)	109	61	331	400	DUN & BRADSTREET (17)	301	391	245
303	COMCAST (20)	162	250	483	295	DUPONT (4)	22	14	35
115	COMERICA (3)	183	349	144	E				
5	COMPAQ COMPUTER (18)	43	39	46					
9	COMPUTER ASSOCIATES (18)	76	272	74	416	EASTERN ENTERPRISES (24)	496	477	434
72	COMPUTER SCIENCES (18)	228	209	282	421	EASTMAN CHEMICAL (4)	316	262	267
277	CONAGRA (10)	133	41	124	471	EASTMAN KODAK (14)	92	82	454
25	CONSECO (17)	216	228	133	162	EATON (9)	250	172	156
299	CONSOLIDATED EDISON (24)	191	183	116	411	ECHLIN (2)	393	314	468
163	CONSOLIDATED NATURAL GAS (24)	305	224	249	127	ECOLAB (6)	371	432	364
161	CONSOLIDATED STORES (8)	380	291	396					



Steve Brazile, Vice President - Business Systems, The Earthgrains Company.

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RANK	COMPANY (INDUSTRY GROUP)	OTHER RANKINGS		
		MARKET VALUE	SALES	PROFITS
298	EDISON INTERNATIONAL (24)	180	140	111
444	EG&G (21)	479	438	445
8	EMC (18)	103	348	141
134	EMERSON ELECTRIC (9)	70	103	72
429	ENGELHARD (16)	419	312	415
329	ENRON (21)	136	51	386
335	ENTERGY (24)	261	138	254
158	EQUIFAX (17)	315	446	327
159	EXXON (11)	4	3	1

F

42	FANNIE MAE (17)	25	29	28
157	FDX (23)	252	104	166
125	FEDERATED DEPT. STORES (8)	196	72	132
79	FIFTH THIRD BANCORP (3)	160	412	185
63	FIRST CHICAGO NBD (3)	85	137	50
369	FIRST DATA (18)	126	238	213
82	FIRST UNION (3)	59	114	44
281	FIRSTENERGY (24)	343	355	222
137	FLEET FINANCIAL GROUP (3)	101	203	62
271	FLEETWOOD ENTS. (13)	460	345	388
380	FLUOR (21)	363	85	359
472	FMC (15)	418	279	462
100	FORD MOTOR (2)	24	2	4
394	FORT JAMES (19)	199	181	387
464	FORTUNE BRANDS (15)	272	256	441
468	FOSTER WHEELER (21)	487	293	457
276	FPL GROUP (24)	181	206	128
45	FREDDIE MAC (17)	61	84	57
300	FREEMONT-MCMORAN C&G (16)	406	404	290
449	FRONTIER (22)	339	380	431
494	FRUIT OF THE LOOM (6)	433	393	488

G

99	GANNETT (20)	104	261	117
17	GAP (8)	111	201	142
190	GENERAL DYNAMICS (1)	306	290	243
41	GENERAL ELECTRIC (5)	1	5	2
491	GENERAL INSTRUMENT (9)	424	426	458
309	GENERAL MILLS (10)	175	219	195
212	GENERAL MOTORS (2)	41	1	5
236	GENERAL RE (17)	119	161	83
403	GENERAL SIGNAL (9)	447	408	366
313	GENUINE PARTS (21)	276	217	220
470	GEORGIA-PACIFIC GROUP (19)	310	100	470

RANK	COMPANY (INDUSTRY GROUP)	OTHER RANKINGS		
		MARKET VALUE	SALES	PROFITS
454	GIANT FOOD (10)	438	292	433
38	GILLETTE (6)	29	132	56
210	GOLDEN WEST (17)	317	350	214
242	GOODRICH (B.F.) (4)	416	323	379
285	GOODYEAR TIRE & RUBBER (2)	177	97	137
325	GPU (24)	325	286	218
264	GRACE (W.R.) (15)	290	328	288
217	GRAINGER (W.W.) (21)	328	287	297
410	GREAT A&P (10)	481	131	404
482	GREAT LAKES CHEMICAL (4)	407	449	407
150	GREEN TREE FINANCIAL (17)	399	429	252
174	GTE (22)	40	43	30
28	GUIDANT (12)	182	448	352

H

43	HALLIBURTON (11)	163	151	160
440	HARCOURT GENERAL (5)	369	301	478
481	HARLAND (JOHN H.) (18)	500	495	449
266	HARNISCHFEGER (15)	461	339	353
366	HARRAH'S ENTERTAINMENT (14)	446	433	384
238	HARRIS (9)	360	299	305
199	HARTFORD FINANCIAL SERVICES (17)	167	93	59
412	HASBRO (14)	330	334	363
23	HBO (18)	178	464	354
46	HEALTHSOUTH (12)	207	342	231
341	HEINZ (H.J.) (10)	96	145	194
66	HELMERICH & PAYNE (11)	471	496	394
399	HERCULES (4)	332	419	234
98	HERSHEY FOODS (10)	201	278	225
92	HEWLETT-PACKARD (18)	20	15	24
146	HILTON HOTELS (14)	242	234	286
44	HOME DEPOT (8)	44	40	70
496	HOMESTAKE MINING (16)	470	491	480
166	HONEYWELL (9)	188	165	154
120	HOUSEHOLD INTL. (17)	142	230	120
250	HOUSTON INDUSTRIES (24)	253	187	176
228	HUMANA (12)	353	169	336
164	HUNTINGTON BANCSHARES (3)	269	386	263

I

74	IBM (18)	12	6	7
379	IKON OFFICE SOLUTIONS (5)	345	233	377
84	ILLINOIS TOOL WORKS (15)	128	240	130
490	INCO (16)	405	378	452
143	INGERSOLL-RAND (15)	235	184	199

Alphabetical List of Companies

The number to the left of the company's name identifies its overall rank among Business Week's Performance Rankings. For an explanation of other rankings, see page 150.

COMPANY (INDUSTRY GROUP)	OTHER RANKINGS			RANK	COMPANY (INDUSTRY GROUP)	OTHER RANKINGS		
	MARKET VALUE	SALES	PROFITS			MARKET VALUE	SALES	PROFITS
I								
INLAND STEEL (16)	489	245	375	223	MATTEL (14)	159	257	266
INTEL (9)	6	35	3	259	MAY DEPARTMENT STORES (8)	138	108	106
INTERNATIONAL FLAVORS (4)	318	441	306	136	MAYTAG (6)	349	321	330
INTERNATIONAL PAPER (19)	135	53	479	123	MBIA (17)	279	492	205
INTERPUBLIC GROUP (21)	270	337	292	6	MBNA (3)	108	282	131
ITT INDUSTRIES (5)	359	152	378	409	McDERMOTT INTL. (15)	441	318	451
				191	McDONALD'S (14)	55	117	49
J				167	McGRAW-HILL (20)	240	317	264
JEFFERSON-PILOT (17)	292	367	191	351	MCI COMMUNICATIONS (22)	62	57	455
JOHNSON & JOHNSON (12)	13	44	18	415	MEAD (19)	378	243	351
JOHNSON CONTROLS (15)	334	116	298	95	MEDTRONIC (12)	80	369	168
JOSTENS (15)	495	486	427	135	MELLON BANK (3)	122	330	108
KAUFMAN & BROAD (13)	490	417	424	211	MERCANTILE BANCORP. (3)	256	390	316
KELLOGG (10)	112	189	136	371	MERCANTILE STORES (8)	428	336	369
KERR-McGEE (11)	389	428	320	15	MERCK (12)	5	42	9
KEYCORP (3)	125	215	89	116	MEREDITH (20)	437	478	403
KIMBERLY-CLARK (19)	64	105	92	19	MERRILL LYNCH (17)	83	22	43
KING WORLD (14)	453	489	356	26	MGIC INVESTMENT (17)	222	483	235
KLA-TENCOR (9)	366	468	358	320	MICRON TECHNOLOGY (9)	262	307	237
KMART (8)	282	20	287	1	MICROSOFT (18)	2	98	12
KNIGHT-RIDDER (20)	327	351	189	453	MILLIPORE (9)	464	485	464
KROGER (10)	179	34	167	178	MINNESOTA MINING & MFG. (15)	58	77	38
				354	MIRAGE RESORTS (14)	357	445	313
L				270	MOBIL (11)	33	8	19
LAIDLAW (23)	326	320	408	302	MONSANTO (4)	65	173	262
LEHMAN BROTHERS HOLDINGS (17)	251	67	125	477	MOORE (18)	472	364	429
LILLY (ELI) (12)	18	155	487	209	MORGAN (J.P.) (3)	93	107	53
LIMITED (8)	234	143	307	10	MORGAN STANLEY, DEAN WITTER (17)	48	33	33
LINCOLN NATIONAL (17)	219	251	447	345	MORTON INTERNATIONAL (4)	348	371	299
LIZ CLAIBORNE (6)	381	373	329	372	MOTOROLA (9)	60	26	66
LOCKHEED MARTIN (1)	88	27	63					
LOEWS (17)	168	52	103	N				
LONGS DRUG STORES (12)	477	346	426	273	NACCO INDUSTRIES (15)	488	385	420
LOUISIANA-PACIFIC (19)	429	374	471	297	NALCO CHEMICAL (4)	417	440	342
LOWE'S (8)	187	130	212	108	NATIONAL CITY (3)	143	283	98
LSI LOGIC (9)	383	451	343	404	NATIONAL SEMICONDUCTOR (9)	365	366	258
LUCENT TECHNOLOGIES (22)	19	32	153	336	NATIONAL SERVICE (9)	432	402	382
				50	NATIONS BANK (3)	42	50	27
M				155	NAVISTAR INTERNATIONAL (2)	444	191	337
MALLINCKRODT (12)	411	394	486	147	NEW YORK TIMES (20)	285	352	279
MANOR CARE (12)	430	444	370	179	NEWELL (15)	255	332	265
MARRIOTT INTL. (14)	202	111	227	407	NEWMONT MINING (16)	340	435	412
MARSH & McLENNAN (17)	130	216	187	425	NIAGARA MOHAWK (24)	456	298	308
MASCO (13)	210	305	198	296	NICOR (24)	451	407	372
				64	NIKE (6)	152	133	105
				275	NORDSTROM (8)	342	248	326

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RANK	COMPANY (INDUSTRY GROUP)	OTHER RANKINGS			RANK	COMPANY (INDUSTRY GROUP)	OTHER RANKINGS		
		MARKET VALUE	SALES	PROFITS			MARKET VALUE	SALES	PROFITS
332	NORFOLK SOUTHERN (23)	147	281	99	262	PPG INDUSTRIES (13)	169	178	115
414	NORTHERN STATES POWER (24)	358	358	293	139	PRAXAIR (4)	239	260	178
31	NORTHERN TELECOM (22)	73	74	97	107	PROCTER & GAMBLE (6)	9	18	14
56	NORTHERN TRUST (3)	220	401	246	33	PROGRESSIVE (17)	224	266	186
58	NORTHROP GRUMMAN (1)	206	147	182	INC	PROVIDIAN FINANCIAL (3)	309	458	321
40	NORWEST (3)	63	141	58	370	PUBLIC SERVICE ENT. GROUP (24)	241	205	134
495	NOVELL (18)	375	481	474	391	PULTE (13)	494	370	436
278	NUCOR (16)	341	284	261	463	QUAKER OATS (10)	243	247	497

O

465	OCCIDENTAL PETROLEUM (11)	217	166	309
30	OMNICOM GROUP (21)	247	338	303
339	ONEOK (24)	486	456	422
102	ORACLE (18)	81	207	113
258	ORYX ENERGY (11)	415	465	338
439	OWENS CORNING (13)	465	275	419
51	OWENS-ILLINOIS (7)	311	263	273

R

247	RALSTON PURINA (10)	186	269	206
197	RAYCHEM (9)	376	422	289
324	RAYTHEON (9)	141	89	145
423	REEBOK INTERNATIONAL (6)	458	311	362
168	REPUBLIC NEW YORK (3)	277	333	163
428	REYNOLDS METALS (16)	337	186	361
48	RITE AID (12)	226	122	284
375	ROCKWELL INTERNATIONAL (9)	161	168	152
272	ROHM & HAAS (4)	287	296	180
67	ROWAN (11)	427	488	346
256	ROYAL DUTCH PETROLEUM (11)	7	7	8
431	RUBBERMAID (15)	346	376	357
475	RUSSELL (6)	492	455	432
420	RYDER SYSTEM (23)	408	252	344

P Q

29	PACCAR (2)	322	192	219
389	PACIFIC ENTERPRISES (24)	402	357	322
337	PACIFICORP (24)	258	208	301
460	PALL (5)	420	473	414
37	PARAMETRIC TECHNOLOGY (18)	238	484	296
59	PARKER HANNIFIN (15)	314	276	238
422	PECO ENERGY (24)	344	265	224
246	PENNEY (J.C.) (8)	110	23	135
358	PENNZOIL (11)	395	362	333
405	PEOPLES ENERGY (24)	475	453	391
384	PEP BOYS (8)	467	406	390
243	PEPSICO (6)	35	48	51
344	PERKIN-ELMER (9)	379	450	416
12	PFIZER (12)	8	106	37
254	PG&E (24)	154	75	110
447	PHARMACIA & UPJOHN (12)	99	193	236
390	PHELPS DODGE (16)	372	300	181
213	PHILIP MORRIS (6)	10	10	6
261	PHILLIPS PETROLEUM (11)	149	76	84
218	PIONEER HI-BRED (10)	271	425	294
105	PITNEY BOWES (18)	145	289	146
485	PLACER DOME (16)	390	462	484
111	PNC BANK (3)	117	200	77
487	POLAROID (14)	448	392	476
478	POTLATCH (19)	476	436	443
401	PP&L RESOURCES (24)	373	340	239

S

241	SAFECO (17)	275	258	173
314	SAFETY-KLEEN (21)	468	475	418
408	SARA LEE (10)	74	56	493
215	SBC COMMUNICATIONS (22)	23	37	52
11	SCHERING-PLOUGH (12)	34	190	55
18	SCHLUMBERGER (11)	54	124	64
32	SCHWAB (CHARLES) (17)	190	354	275
373	SCIENTIFIC-ATLANTA (22)	473	460	413
452	SEAGATE TECHNOLOGY (18)	293	164	472
363	SEAGRAM (6)	146	109	226
248	SEARS, ROEBUCK (8)	94	16	65
78	SERVICE CORP. INTL. (21)	200	372	203
141	SHARED MEDICAL (18)	454	480	421
187	SHERWIN-WILLIAMS (13)	297	253	280
220	SIGMA-ALDRICH (12)	361	471	340
426	SILICON GRAPHICS (18)	412	308	446
244	SNAP-ON (15)	421	427	350
305	SONAT (24)	374	285	334
263	SOUTHERN (24)	114	102	78



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RANK	COMPANY (INDUSTRY GROUP)	OTHER RANKINGS		
		MARKET VALUE	SALES	PROFITS
68	SOUTHWEST AIRLINES (23)	284	302	241
443	SPRINGS INDUSTRIES (15)	484	387	411
226	SPRINT (22)	68	78	85
402	ST. JUDE MEDICAL (12)	384	476	430
133	ST. PAUL (17)	249	210	107
459	STANLEY WORKS (15)	350	361	465
35	STATE STREET (3)	194	343	200
493	STONE CONTAINER (7)	483	255	490
54	SUMMIT BANCORP. (3)	215	383	207
346	SUN (11)	410	127	278
20	SUN MICROSYSTEMS (18)	107	142	114
34	SUNAMERICA (17)	212	457	177
140	SUNTRUST BANKS (3)	124	270	123
175	SUPERVALU (10)	409	68	295
70	SYNOVUS FINANCIAL (3)	291	469	341
232	SYSCO (10)	231	80	242

TU

338	TANDY (6)	336	231	324
350	TEKTRONIX (9)	439	400	409
376	TELE-COMMUNICATIONS (20)	129	195	489
7	TELLABS (22)	176	463	277
458	TEMPLE-INLAND (7)	382	313	435
307	TENET HEALTHCARE (12)	173	139	460
234	TENNECO (5)	263	182	210
124	TEXACO (11)	66	12	32
364	TEXAS INSTRUMENTS (9)	89	134	250
301	TEXAS UTILITIES (24)	198	167	119
149	TEXTRON (5)	158	126	138
138	THERMO ELECTRON (9)	289	316	291
128	THOMAS & BETTS (9)	398	395	348
INC	3COM (18)	153	226	335
240	TIME WARNER (20)	53	94	253
239	TIMES MIRROR (20)	307	327	285
200	TIMKEN (15)	449	365	339
21	TJX (8)	283	177	247
198	TORCHMARK (17)	278	381	217
330	TOYS 'R' US (8)	245	121	149
268	TRANSAMERICA (17)	254	223	143
16	TRAVELERS GROUP (17)	27	17	26
77	TRIBUNE (20)	232	360	192
INC	TRICON GLOBAL RESTAURANTS (14)	347	135	473
430	TRW (5)	273	123	467
462	UPPERWARE (15)	463	454	398
INC	TYE INTL. (15)	71	NR	NR

RANK	COMPANY (INDUSTRY GROUP)	OTHER RANKINGS		
		MARKET VALUE	SALES	PROFITS
101	U.S. BANCORP (3)	69	204	96
387	U.S. SURGICAL (12)	434	467	392
441	UNICOM (24)	264	185	482
INC	UNILEVER NV (10)	50	NR	NR
413	UNION CAMP (19)	354	271	399
222	UNION CARBIDE (4)	300	202	121
347	UNION PACIFIC (23)	156	119	172
353	UNION PACIFIC RESOURCES (11)	303	414	228
419	UNISYS (18)	397	196	495
189	UNITED HEALTHCARE (12)	174	113	157
151	UNITED TECHNOLOGIES (1)	97	38	76
172	UNOCAL (11)	205	213	122
205	UNUM (17)	259	294	208
14	US AIRWAYS GROUP (23)	298	156	79
185	U S WEST COMMUNICATIONS (22)	77	129	67
386	U S WEST MEDIA (20)	102	246	491
442	USF&G (17)	414	322	319
323	UST (6)	280	443	170
267	USX-MARATHON GROUP (11)	193	73	159
225	USX-U.S. STEEL GROUP (16)	403	188	162

V W X Y Z

252	VF (6)	294	239	215
181	VIACOM (14)	118	96	204
216	WACHOVIA (3)	157	280	129
109	WAL-MART STORES (8)	11	4	16
76	WALGREEN (12)	106	88	165
60	WARNER-LAMBERT (12)	52	162	94
86	WASHINGTON MUTUAL (17)	113	175	151
483	WASTE MANAGEMENT (21)	165	144	498
204	WELLS FARGO (3)	72	146	71
367	WENDY'S INTL. (14)	422	398	367
154	WESTERN ATLAS (11)	355	430	395
450	WESTVACO (19)	388	347	345
445	WEYERHAEUSER (19)	192	118	221
451	WHIRLPOOL (6)	319	154	466
467	WILLAMETTE INDUSTRIES (19)	356	319	405
85	WILLIAMS (24)	185	273	216
304	WINN-DIXIE STORES (10)	230	90	310
349	WOOLWORTH (8)	392	198	311
180	WORLDCOM (22)	57	179	197
398	WORTHINGTON INDS. (16)	462	397	393
235	WRIGLEY (WM.) JR. (10)	214	409	274
121	XEROX (18)	67	65	54

A close-up portrait of David Brinkley, an older man with white hair, wearing a dark suit, white shirt, and a red tie with a small pattern. He is looking slightly to the left of the camera with a thoughtful expression. The background is dark and out of focus, showing some vertical lines that might be window frames.

“For more than
50 years, I’ve reported
on change.”

“I’ve seen world leaders come and go, I’ve seen governments crumble and borders redrawn, and through it all I’ve noticed that the only thing that doesn’t change is people. We’re still all more alike than we are different.

“I’ve always felt the best way for nations to keep the peace is to supply people with food, not weapons. Back in the 1950s, President Eisenhower said, ‘Every gun that is made, every warship launched, every rocket fired signifies...a theft from those who hunger and are not fed.’ Eisenhower was a true champion of change.

“Feeding the world is one way to make sure things change for the better.”

INTELLIGENCE BRIEFINGS

a special advertising series sponsored by CONSECO

The following article appears on S&P Personal Wealth, www.personalwealth.com, the interactive investment advisory service for the individual investor:

PREPARE NOW FOR PROPOSED ESTATE TAX LAW CHANGES

Here's a heads-up for those who have built up substantial estates (and after a seven-year bull market, that's a lot of people): the Clinton Administration has proposed eliminating a number

as part of a majority interest. But the Administration says the deal should apply only to active businesses, not to passively appreciating assets. In its present form the change would apply only to transfers made after the date of enactment, *so if a family LP fits with your estate planning goals, play safe and set one up soon.*

Crummey trusts are also in jeopardy. The Treasury would overrule a 1968 court decision that allowed assets transferred to a trust to qualify for annual gift tax exclusions (up to \$10,000 or \$20,000

h i g h l i g h t s f r o m S & P P e r s o n a l W e a l t h

of the most popular ways to reduce taxes on assets transferred to heirs. While the Republican-controlled Congress wants to lower estate taxes, not raise them, any of the clampdowns noted here could become law, if not this year possibly later on.

As proposed by the Treasury, none of them would be retroactive, and while Congress could change that, estate owners may want to set up one or more of the asset-transfer vehicles involved right away in case the tax axe falls.

Family LPs. The most far-reaching of the proposed tax changes would eliminate family limited partnerships, which have become a popular way to reduce estate taxes on assets passing to children or other heirs. You contribute assets to a partnership and give shares to your children. The main tax break results from setting lower values on the limited-partner shares than the value of the property they represent.

The IRS now allows such valuation discounts on the assumption that a minority interest in a business has less value than the same shares would have

with a spouse). The case established a trust beneficiary's right to make limited distributions of trust assets. The right gives the beneficiary a "present interest" in the assets, which makes them a gift.

The Administration would not recognize transfers to Crummey trusts as gifts after 1998. *Grantors of existing Crummey trusts may want to begin investigating alternative transfer vehicles*, such as gifts that comply with state uniform gifts to minors statutes.

Personal residence trusts are an efficient way to reduce gift and estate taxes. A couple or a surviving spouse transfers a personal residence to children or other heirs and continues living in it, making sure the IRS will recognize it as "a current gift of future interest." Gift tax is paid on the value of the property, but the value is substantially reduced by the donor's retained interest, and no further tax is paid on the gift or its subsequent appreciation.

The Treasury wants to redefine the donor's retained interest in order to eliminate the personal residence trust tax advantage. If it does become law, *early birds transferring their nests ahead of time will benefit.*



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SHOWMEN

THE APOSTLE OF LIFE INSURANCE



Joe Plumeri runs PFS with evangelistic fervor—and charging these prices, he has to

The moment Joseph J. Plumeri II bounds into the spotlight at the Philadelphia Convention Center, the crowd erupts in a raucous ovation. No doubt many of the 4,500 people on hand have caught his act before. nattily attired in grey pinstripes with matching tie and pocket square, he plants himself center stage and opens his arms in a hey-look-me-over gesture. "He's a stud," someone shouts as Plumeri, a short, stocky 53-year-old, saunters stage right in super-slow motion. "It's a cool walk," he says, getting a big laugh. "I learned it in the old neighborhood."

That would be the blue-collar precincts of North Trenton, N. J., just 15 miles from here. The cool-walking

demonstration ended, Plumeri explains how he stumbled into a career on Wall Street by taking a menial job at a brokerage house that he had mistaken for a law firm. He tells his tale with brio, working it for laugh after laugh. Finally, he lets the hilarity fade. "I tell you this because it's O. K. to be embarrassed, it's O. K. to have childlike enthusiasm," he says softly. Plumeri pauses and then looses a full-throated cry: "Don't live your life without having a dream. Otherwise, you've wasted it. O. K.? Are you with me?"

As the crowd roars its assent, Plumeri flashes a dazzlingly toothy grin, clenches one hand into a fist, and thrusts it over his head. Hail the conquering hero, returned home a multimillionaire!

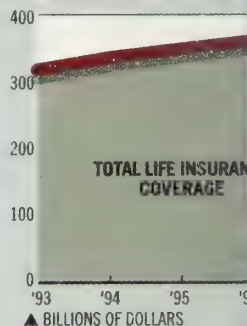
When it comes to motivational speaking, the likes of Tony Robbins and Stephen R.

Covey have nothing on Joe Plumeri. But unlike these marquee names of the self-help trade, Plumeri does not hawk books and tapes for a living. He took home at least \$3 million in salary and bonus last year as a senior executive of one of America's largest companies, Travelers Group Inc.

Corporations don't come any more substantial than Travelers, a \$27 billion financial-services giant that is one of

A FINANCIAL SUPERMARKET FOR THE MASSES

Primerica's fastest growth comes from products other than life insurance



DATA: PFS, TRAVELERS GROUP

the 30 stocks in the Dow Jones industrial average. But as chairman and chief executive of the Primerica Financial Services (PFS) division of Travelers, Plumeri runs one of the most eccentric—and controversial—operations in consumer finance. “This is not a company where you just work,” Plumeri says. “You have to believe.”

In some ways, belief in PFS would seem misplaced. Every year, the company, based outside Atlanta, recruits thousands of working folk—cabdrivers, schoolteachers, factory workers—into part-time positions in its sales force. Most sell a life-insurance policy or two and call it quits. Although PFS boasts one of the largest captive sales forces in finance, only 41% of its 80,000 sales reps have been with the company more than two years. Yes, you have to believe to make it at PFS, because the odds against success are so steep that logic argues against even making an effort.

But if the PFS sales force is volatile, it also is highly productive, even though PFS charges some of the highest rates around. Compared to a widely used pricing service, 20-year term policies by the pre-charged per \$500,000 of coverage. In reckoning, Old Republic Life Insurance offers consumers the best deal, at \$775. (PFS is introducing a new policy, priced at \$695.)

Nevertheless, last year PFS was second among all insurers in the face value of policies sold, at \$52.6 billion—all of it

term insurance. Most insurers specializing in term depend on direct-mail solicitation and aggressive price discounting to attract buyers. But PFS employs an intensely personal approach—neighbor selling to neighbor across the kitchen table.

What's more, since Plumeri took over in late 1994, PFS also has generated sharply rising sales of such other financial staples as mutual funds, variable annuities, consumer and home-equity loans, and auto and homeowner's insur-

CEO PLUMERI

“I am an emotional person with a lot of drive, and that has caused some problems in my career. But I come from the view that you've got to be yourself”



ance (charts). “Whenever I need to feel better, I go down to Atlanta,” says Sanford I. Weill, Travelers' CEO. “PFS is important to everything we do.”

You wouldn't know it just from looking at the numbers. PFS's record \$335 million in operating profits in 1997 amounted to just 10% of Travelers Group's total. But Weill sees PFS as the template for one of the most elusive ambitions of his long career as a corporate builder: to mold a diverse group of financial companies into a tightly woven, symbiotic whole—into a financial supermarket, in other words.

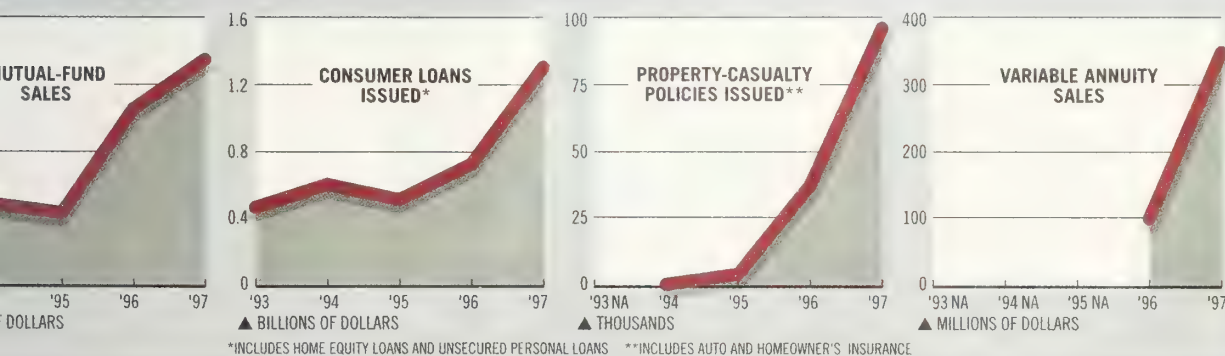
To this end, PFS doesn't just sell, it cross-sells. Almost every one of the financial wares it offers is custom-made for it by another Travelers subsidiary. This enables PFS's sister companies to tap into a market of lower-income customers while keeping the profits gener-

ated all in the Travelers family. As with term insurance, PFS's other offerings tend toward the pricey.

Although PFS unquestionably is on a roll, its continued success is by no means foreordained. In many ways, this remains a company in transition from a legacy of tumult and notoriety. And although Plumeri of late has won admirers inside and outside Travelers, he is an emotionally combustible man with a somewhat uneven track record of his

own to transcend. “I am an emotional person with a lot of drive, and that has caused some problems in my career,” Plumeri concedes. “But I come from the view that you've got to be yourself, for better or worse. And what got me where I am today was my emotion.”

LUCKY MISTAKE. A third-generation Italian-American, Plumeri grew up in an ethnically mixed middle-class neighborhood in North Trenton. After graduating from the College of William & Mary with mediocre grades, he accepted the only job offer he got: teaching history at a high school in rural Pennsylvania. Plumeri quit after two years and, for lack of a better idea, enrolled in 1966 at New York Law School in lower Manhattan. He promptly went in search of part-time work and landed a clerking job at Carter, Berlind & Weill, the brokerage he mistook for a law firm. Plumeri took to



the securities business with such enthusiasm that he soon dropped out of law school to make a career on Wall Street.

As Weill's little firm metamorphosed into Shearson Loeb Rhodes, Plumeri rose through its retail ranks. Admired as one of the firm's hardest-working and most market-savvy managers, he also was resented as a temperamental self-promoter. "I continually had to urge Joe to let others into the spotlight," says Hardwick Simmons, who was Plumeri's boss at Shearson and is now CEO of Prudential Securities Inc. "But he never did. He couldn't. When most people want to revive themselves, they take a vacation. Joe puts on a show."

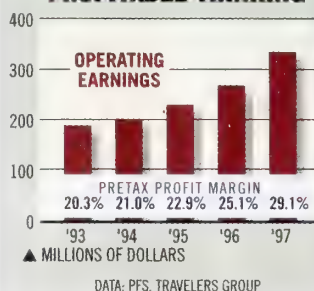
When Shearson ran into serious financial trouble in the late 1980s, American Express Co. tightened its grip on the firm, which it had acquired in 1981. All of Shearson's top home-grown executives quit or were pushed out except

Sandy shed a tear, too."

Plumeri only lasted a year in the job to which he'd aspired his entire career. In August, 1994, Weill abruptly removed him and made him a vice-chairman of Travelers (a title he still holds). Weill declines to comment, but Plumeri says that he was dismissed because he was generally uncooperative in dealing with fellow Smith Barney executives. "I was so intent on getting the job done that I eliminated the input of other people," he says, sounding more wistful than penitent. "If I'd done better at nurturing relationships, who knows how it would have turned out?"

After two months in career limbo, Plumeri was put in charge of PFS. As a

THE POWER OF PROFITABLE THINKING



million, lives in Tennessee and bestride a hierarchy of 15,680 reps that stretches from Massachusetts to Hawaii. Meanwhile, at the bottom of the pyramid, reps come and go so fast that Atlanta may never even know the names. "This is a business you can't manage," says John Addison, a 16-year PFS veteran who moved up to president under Plumeri. "You gotta lead it."

Plumeri runs PFS in what might be called continuous campaign mode. He gives 10 to 20 speeches a week on average as he travels the country rallying PFSers in groups large and small. His Philadelphia appearance last August was just one stop in a 14-city tour of North America that culminated just before Christmas in a roof-rattling performance before 30,000 at PFS's annual convention in St. Louis. Plumeri also hosts his own monthly TV talk show, which is beamed from PFS headquarters by satellite to thousands of agents nationwide.

ATOM BOMB. As a showman-CEO, Plumeri is following in the footsteps of PFS founder Arthur L. (Art) Williams Jr., a self-described "country boy" from Georgia who began selling life insurance part-time while working as a high school math teacher and football coach. In 1977, Williams set up his own agency, A. L. Williams Corp., which is the insurance industry like an atom bomb. By the mid-1980s, A. L. Williams had assembled a sales force of 190,000 and was writing new policies at the rate of \$90 billion a year—double the volume of longtime industry champion Prudential Insurance.

How did Williams do it? For a start, he put A. L. Williams at an enormous tactical advantage by only selling term insurance in an era of galloping discount with whole life, the predominant but more costly type of policy. (Whole life combines a death benefit with a savings account.) Second, Williams had rare talent for inspiring working-class folk to feats of fanatic salesmanship. His slogan—"Buy Term and Invest the D



one: Joe Plumeri, who in 1990 succeeded Simmons as retail brokerage chief. Even so, Plumeri fought constantly with the white-shoe investment bankers and AmEx smoothies who now controlled Shearson. "The clash in styles was surreal," says one senior AmEx executive. "Joe did a lot of yelling and shouting, a lot of chest beating."

Plumeri's ordeal ended happily in 1993 when Weill bought Shearson back from American Express and merged it into Smith Barney. The day before the transaction was announced, Weill summoned Plumeri to his Manhattan apartment and offered him the presidency of Smith Barney. "That was the most satisfying moment of my life," recalls Plumeri. "I cried—as usual—and I remember that

TRUE BELIEVER

Says Mosquera, whose PFS income has risen from \$4,424 in 1992 to \$252,261 in 1997: "Mr. Plumeri put us into the 21st century"

multilevel marketing organization, PFS is closer in spirit and in structure to Amway than Allstate. Salaries are rare at PFS. Even full-time agents work strictly on commission and must cover their own expenses. Under PFS's commission system, agents are rewarded for building their own "hierarchies" by recruiting new reps to the force.

In fact, top-level PFS agents no longer need to do much selling because they

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ference"—became the rallying cry of a populist crusade against the life-insurance Establishment. "When I take my last dad-gum breath," Williams famously declared, "I want to be kicking Prudential's butt."

Williams and his legions replaced tens of thousands of whole-life policies with term, thus depriving rival insurers of a king's ransom in future premium payments. The big life companies screamed foul, denigrating Williams' sales reps as ill-trained amateurs who used deceptive sales practices. Although many state regulators investigated A. L. Williams, the company escaped with only minor reprimands and fines.

Even so, observers were stunned when Weill bought a majority stake in A. L. Williams in 1988. Why would Weill, a much-admired figure in Corporate America, get in bed with a wild man like Art Williams? In truth, Weill was enamored not of Williams but of his sales force, which he saw as a unique pipeline into Middle America. Weill gradually shouldered Williams to the sidelines but did not gain full control until mid-1990, when word leaked that the FBI was investigating allegations that Williams had sabotaged a group of his agents who had defied his wishes and gone into business for themselves. Williams took a leave of absence from which he never returned, even though he was not indicted.

REANIMATOR. Weill dispatched a series of executives from headquarters to run PFS, but none could match Williams' charisma quotient. Agents deserted in droves. By the time the company finally was stabilized in 1994, the sales force had shrunk to 98,000 from a peak of 190,000 in 1988. To reanimate the listless operation, Weill turned to Plumeri. Explains Weill: "I knew that Joe had a high energy level and was an incredible communicator to audiences of all sizes."

Unlike Williams, Plumeri came to PFS well schooled in the fundamentals of corporate management. He imported former Shearson colleagues to fill a half-dozen key posts and drew heavily from his Wall Street experience in imposing a more demanding training regimen for reps and adopting stricter rules gov-

erning sales practices. "PFS now has one of the strongest compliance programs in the industry," says Michael F. Albanese, a vice-president of A. M. Best Co., which rates insurance companies.

Equally important, Plumeri reorganized PFS's sales and marketing around a computer-generated financial plan called the Financial Needs Analysis, which outlines products that might be right for the customer. The FNA is nothing special; many brokers and insurers offer something similar. But the FNA was critical to Plumeri's transformation of PFS in

morality: Travelers sells to the affluent PFS to the working class. "For the average person, I do think that term is better deal," Plumeri says.

If PFS is no longer quite the industry pariah that it was in Williams' heyday, will continue to raise Establishment hackles as long as it keeps replacing whole-life policies with term. "I'm willing to concede that Plumeri is trying to curb some of the excesses, but this is still an organization that lives by the myth that all permanent life policies should be replaced," says Alan Press, a Guardian Life Insurance Co. agent and longtime PFS critic. "In spirit this is still Art Williams company."

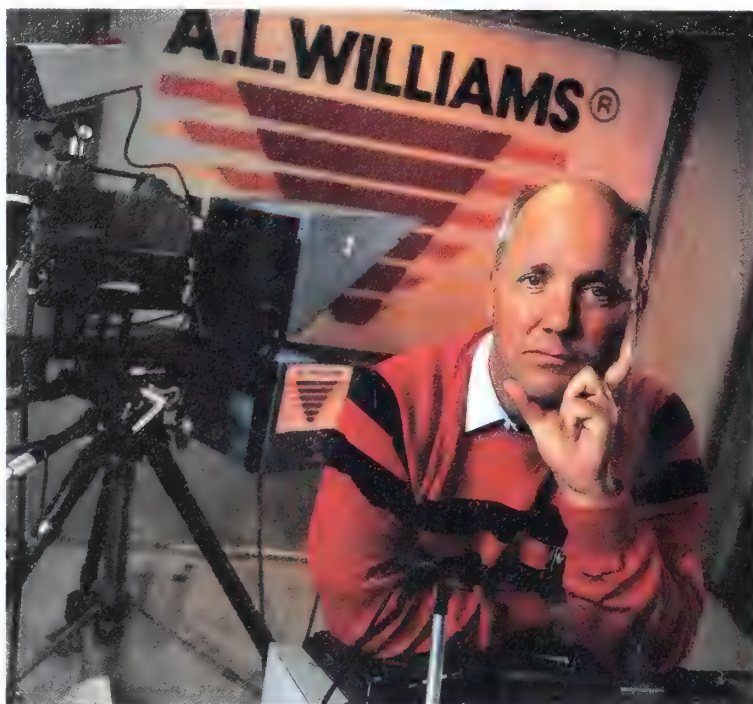
A BUSINESS WEEK reporter recently attended a PFS recruiting session in the New York City area that began with a 20-minute video of Williams speaking to the National Religious Broadcasters in 1987. "That surprises me," Plumeri says, "but I'd argue that can't be going on at a lot of offices. He founded the company and I give him every ounce of respect for it. But this is a business looking forward, not a cult of personality living in the past."

But if the Williams aura is fading, PFS remains a prisoner of the

pricing structure he created. To generate sufficient cash to pay a half-dozen levels of commissions on a single sale, PFS must continue to defy the odds by selling commodity goods at premium prices. Although Plumeri's emphasis on financial planning lays the groundwork for a much bigger company, it also is educating its customers to an extent that may undermine PFS in the long run for the simple reason that price tends to matter far more to the well-informed financial consumer than the ignorant one.

But it is Plumeri's nature to accentuate the positive. And why not? He's back in the good graces of Weill and playing to the biggest crowds of his career. "We have an opportunity to cross-sell as far as the eye can see," he says. No one who knows Plumeri doubts his energy or his drive. The question is whether he can continue to keep his ego and emotions in check now that he is what he's always longed to be: a star.

By Anthony Bianco in New York



FOUNDER WILLIAMS

PFS's original showman famously declared: "When I take my last dad-gum breath, I want to be kicking Prudential's butt"

two ways: It aided his compliance crackdown by scripting an agent's early dealings with a client while establishing a conceptual foundation for cross-selling. "Mr. Plumeri put us into the 21st century," says David J. Mosquera, a former mechanical engineer whose PFS income has risen from \$4,424 in 1992, his first year as a rep, to \$252,261 in 1997.

One thing PFS still doesn't offer is whole life. Unlike Williams, Plumeri does not frame the term vs. whole-life debate in terms of good and evil. How could he, when PFS's sister company, Travelers Life & Annuity, is a top whole-life vendor? To Plumeri, it's an issue of market segmentation, not

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It's called "nuclear lava." Fortunately, the hellish stuff exists in only one place: Chernobyl. After the No. 4 nuclear reactor blew its top on Apr. 26, 1986, tons of scorching nuke fuel oozed from room to room, consuming cement, melting steel pipes, and contaminating everything in its path. With time, the mess cooled and congealed. Today, a floor of rock-hard, radioactive lava marks history's worst nuclear accident.

In places, the lava wells up eerily from the floor. One such "stalagmite"

looks like an elephant's foot. Curiosity is dangerous, though. Every second you linger, you're getting zapped by radiation. Even quick visits in protective suits can mean soaking up 30 rads (a unit of radiation exposure). That's about 100 times the dose most people get in a year from X-ray exams and sunlight. But Chernobyl workers regularly brave the danger to monitor conditions inside.

Despite their daring, the workers haven't been able to keep up with the deterioration of the concrete-and-steel

sarcophagus that was hastily thrown over the reactor 12 years ago. It is now sinking into the wreckage. The vault is cracking and rain seeps in, creating radioactive ponds that threaten the water table. And when the wind picks up, workers have to spray chemicals on the debris inside to keep radioactive dust from being blown into the atmosphere. Left untended, the structure could collapse, unleashing another deadly cloud of radiation over the Ukrainian countryside some 75 miles north of Kiev. So the Group of Seven has pledged \$758 million to reinforce the tomb. The job will take years—and would surely claim many lives if done exclusively by humans.

VALIDATION. Instead of sacrificing more lives, robots will handle the repair. That's turning Chernobyl into a testing ground for new robot technology, because the machines able to withstand its invidious radiation will be top contenders for many future cleanup tasks. Nuclear reactors built in the '70s will begin reaching the end of their design lives in the

IN THE VAULT
Maintaining the reactor's steel-and-concrete sarcophagus is so costly that the Group of Seven is chipping in

2010s and will need to be dismantled. By 2030, some 40 plants will probably be decommissioned. Each could require a small army of robots that spends years on the task—further swelling the reviving market for

these steel-collar workers. "Everyone wants a chance to validate their technologies" at Chernobyl, says Maynard A. Holliday, an investigator at the Energy Dept.'s Lawrence Livermore National Laboratory in Livermore, Calif.

The potential demand adds more luster to these mechanical marvels, which have staged a dramatic turnaround. In the 1980s, robot sales headed downward. They bottomed out in 1987 at \$299 million. For the next six years, the market bounced around in the \$400 million range. Since 1993, though, robots have been coming back. Last year, shipments squeaked past the \$1 billion mark for the first time in the U.S. Much of the market is for factory robots. But it includes so-called field robots—such as the one being developed for Chernobyl—designed for all sorts of hazardous tasks, such as repairing offshore oil rigs and inspecting underground storage tanks (table, page 170).

There will also be glamour work for mobile robots in space, which is "hot" because there's no atmosphere to screen radiation from the sun. An early er-

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deavor could be constructing the international space station, once its materials are launched late this year and next. And future NASA missions call for robots to explore other planets, mine asteroids, and maybe build a moon base.

Chernobyl will test the mettle of the toughest machines, though. Intense radiation is lethal for ordinary silicon chips, so the computer brains and sensors commonly found in robots won't do. The first company to get a crack at Chernobyl will be Pittsburgh-based RedZone Robotics Inc., a spin-off from Carnegie Mellon University. RedZone's engineers are putting together Pioneer, a \$2.7 million robot funded by NASA and the Energy Dept. that moves on tank tracks and carries various radiation-hardened equipment.

Pioneer should roll into the Chernobyl sarcophagus sometime this summer to map the lava's radioactivity and make stress tests on the shelter. The information will help Chernobyl officials plan the immense job ahead—first, shoring up the vault, and eventually removing the lava.

If Pioneer performs well, it promises to be the basis for a new generation of muscular construction robots to be manufactured in Ukraine. The technology will be given to a Ukrainian startup that can engage local nuclear weapons scientists. They will create newer and better machines—and, it is hoped, resist the temptation to sell their services to aspiring nuclear powers.

TOY STORY. Still, many Ukrainian officials are cool to the U.S. robotics push. In the drab brick buildings around the entombed reactor, Chernobyl's managers complain that Americans, their eyes on missions to distant planets, are foisting unnecessarily complex technology on Ukraine. "For me, the robot is just an expensive toy," grumbles deputy director Valentin Kupny. "I don't need it."

While anxious to protect their children from radioactivity, the Ukrainians have special respect for the workers who regularly dart into the wreckage to

snap pictures or measure the accumulating rainwater. Technician Sergei Koshelov ventures in several times a month. "The main thing is, you have to get out fast," he says. Deputy manager Artur Korneev, who decorates his office with photos he took in the reactor's poisonous central hall, doubts Pioneer can improve upon the work already done by humans.

Chernobyl's caretakers also worry about costs. Maintaining the tomb for Reactor No. 4 is taxing Ukraine's meager cash resources. The Ukrainians

rushing about with a camera, the 1,000-pound robot, designed to withstand a staggering 1 million rads, can explore 12,500 square meters of Chernobyl. Dragging a 100-meter power and remote-control line, it will push its way through the rubble behind a small bulldozer blade, clearing paths that will also help people dash in and out faster.

The robot will send back streams of information, including visual images. The Livermore team that devised the vision system for the Pathfinder robot, which gave humans new visions of Mars,

is creating a "rad-hard" version for Pioneer. At researchers at the University of Iowa's Ames Research Center are preparing a "smart" coring arm that will extract samples of the concrete structure. As this tool bores into a surface, it measures the force required and analyzes the material's chemical composition. Later, NASA may use the coring arm to drill into a comet.

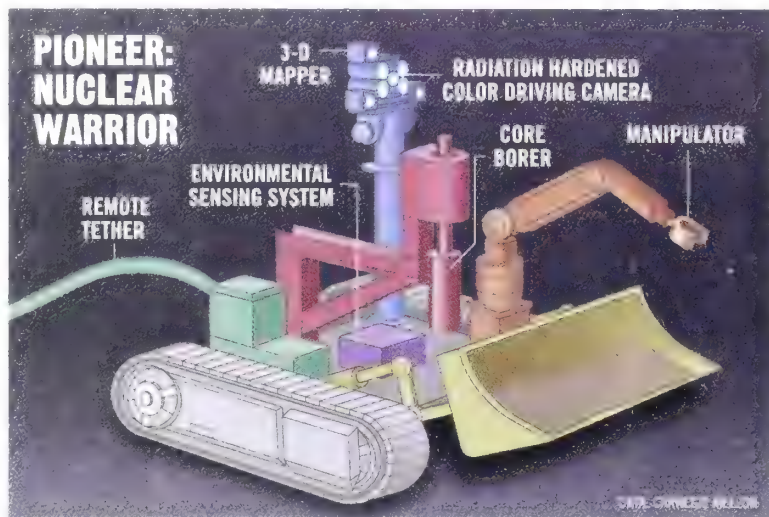
The Chernobyl data will be compiled in a 3D map. With mouse clicks, engineers will be able to read chemical composition, temperature, radiation levels, and structural strength at almost any particular spot—an invaluable aid for planning the massive shelter repair work ahead.

For RedZone, the project is a long-delayed homecoming of sorts. The company was created following the 1986 Chernobyl disaster, when a group of Soviets fled to Pittsburgh and asked William L. "Red" Whittaker for robots like the ones that Carnegie Mellon

built for the Three Mile Island cleanup. Whittaker founded RedZone to provide the technology—but ran afoul of U.S. government controls on high-tech exports to the Soviet Union.

So RedZone turned to building robots for the nuclear industry. It has been a small but steady business. But now RedZone's technology braves the killer rads of Chernobyl, it could be in high demand for hazardous chores.

By Stephen Baker in Pittsburgh and Carol Matlack in Chernobyl



WHERE HUMANS FEAR TO TREAD

State-of-the-art mobile robots could help clean up Chernobyl, and there are many other potential applications for these rugged machines:

- Inspection and repair of nuclear power stations
- Maintaining nuclear reactors in naval ships and submarines
- Checking underground storage tanks and pipelines for leaks
- Site surveys and cleanups of hazardous-waste dumps
- Detecting and disposing of bombs and other terrorist weapons
- Deep-sea research and maintenance of offshore oil rigs
- Exploring the surface of planets and mining minerals on asteroids
- Constructing the space station and a base on the moon

were dismayed late last year when they learned that the cost of Pioneer was to come out of Washington's \$78 million contribution to the G-7's rehabilitation plan. The Ukrainians wanted to cancel the robot and restore the \$2.7 million. "It was almost a showstopper," admits Timothy Denmeade, RedZone's business development manager. Washington agreed to fund the robot separately.

RedZone's engineers hope the Ukrainians will learn to love Pioneer once they see it in action. Unlike a human

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EDITED BY CATHERINE ARNST

KE, SHAKE, KE YOUR IT TREE

THE JERRY LEE LEWIS OF pickers. An engineer at the Agriculture Dept., in partnership with a company that makes berry-picking equipment, has developed a machine that shakes the branches of citrus trees so the fruit falls off—cutting harvesting costs by two-thirds.

Most citrus fruit is still picked by hand, a process that can cost growers for each 90-pound box of fruit. Mechanical shakers have been developed, but a chemical fruit loosener must be sprayed on the trees, and no chemical has been approved for this use. Agricultural Research Service engineer Donald L. Peterson, working with Blueberry Equipment Inc. of Farmington, Mich., has developed a leaf shaker. The machine looks something like

a giant hairbrush with nylon bristles 12 feet long. The bristles reach into a tree's canopy and gently rotate and shake until the fruit falls.

Peterson tested the machine in Florida citrus groves over the past two seasons and says it harvested seven to nine trees per minute, up to 15 times faster than hand labor. And the cost was only 50¢ per 90-pound box. Turner



WINDFALL: The shaker harvested 15 times faster than hand labor

Foods Corp., a subsidiary of Florida Power & Light Group that grows 18,000 acres of oranges, is now working with Blueberry Equipment to develop a commercial machine for next season. Could be the start of a whole lotta shakin' goin' on. □

NOT BE ALARMED—UNNECESSARILY

THE WAKE OF THE 1996 ValuJet crash, in which two engines failed, led to new regulations. Federal Aviation Administration required that all aircraft have fire detection and suppression systems in their cargo holds. But many current systems are outdated and set off far too many false alarms. One recent study showed that 562 of the 572 aircraft that went off on fire alarms over the past 12 years were false. Microsafe Flight Safety Systems in Bellingham, Wash., may have a solution—a highly accurate system for spotting and

dousing fires that was first developed in 1994 for buses. "Then came ValuJet, and we saw an immediate market in aviation," says Chief Executive Patrick Golden. His system links 10 sensors for smoke, temperature changes, and flame to a powerful microprocessor. If one sensor spots something amiss, the processor analyzes signals from all the others to see if the fire is real, cutting the false alarm rate almost totally. Microsafe says the system has been ordered for a turboprop airplane that's still in development. John Carey

PUTTING BRAINS IN PLANE WINGS

PLASTICS REINFORCED WITH CARBON FIBERS ARE LIGHT and durable—very desirable if you are building an aircraft wing or fuselage. But the virtues of these composites go beyond weight and strength, says Deborah Chung, professor of mechanical and aerospace engineering at the State University of New York at Buffalo. The composites could also someday be fabricated into giant arrays of solar cells, temperature sensors, and other semiconductor devices.

First, Chung says, the carbon fibers must be "doped" with chemicals that boost electrical conductivity. Then, by alternating layers of carbon fibers with layers of insulating material, engineers could create airplane wings or automobile body panels that would function as solar arrays, converting sunlight to electricity and storing it.

Chung's concept, presented at the International Symposium on Smart Structures and Materials in San Diego earlier this month, is a radical departure from conventional approaches, which embed tiny electronic or optical devices in the "smart" material. Here, says Chung, "we can use the structural materials themselves as the electronics." This approach would preserve the integrity of the materials and eliminate the need for expensive embedded chips.

Neil Gross

IN SURGERY, A LITTLE DAB'LL GLUE YA

EVEN THE MOST SKILLED OF surgeons dread the leaks that can develop around incisions after patients have been stitched up with sutures or surgical staples. Focal Inc. in Lexington, Mass., is proposing to close them up with a dab of glue. Focal's synthetic surgical sealant expands and contracts with the tissue it adheres to and takes about a year for the body to absorb. The sealant, based on patented chemistry from the University of Texas at Austin, is a clear gel with the consistency of syrup. After putting in staples or sutures, surgeons drip the sealant along the incision, then harden it with a blast of special-wavelength light.

"If we can seal air leaks, the potential for in-

fection goes way down, and patients won't have to stay in the hospital as long," says Dr. Larry R. Kaiser, a professor of surgery at the University of Pennsylvania, where clinical trials are being conducted. Focal's product has been approved for use in lung surgeries in Europe, and Johnson & Johnson has agreed to pay Focal \$18 million for marketing rights to the sealant outside the U.S. The glue "will be expensive," says David M. Clapper, Focal's president and chief executive. "But most people spend \$1,000 and up each day they are in the hospital."

Paul C. Judge



CLEAN SEAL: The surgical glue may cut potential for infections

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THE CITY OF LONDON

It has reclaimed its status as a global financial mecca

A year ago, Timothy Grell was working in Merrill Lynch & Co.'s Wall Street offices, dreaming up creative financing packages. Now his lanky frame can be found on the fixed-income trading floor of Merrill's sprawling European headquarters in the City of London. Leading a 19-member team, he's preaching the virtues of junk debt to a receptive audience of European companies and fund managers. Since April, 1997, when Merrill introduced the first European currency junk bond for Geberit Group, a Swiss maker of plumbing supplies, "the market has really taken off," says Grell.

Grell is one of thousands of financial professionals from the U.S., Asia, and Europe who are flocking to the City, the financial district in the ancient heart of London. Like the Barings, who came to Britain in the 18th century from Bremen, and Nathan Mayer Rothschild, the Frankfurter who called the tune in the City in the early 19th century, these new financiers bring much-needed ideas. This time, the charge is being led by U.S. banks and investment houses, which are using their record profits on Wall Street to pave the way for aggressive expansion abroad. Followed closely by European institutions that see their future in investment banking, these financial giants are bringing a massive infusion of capital and technology to a City that until the late 1980s was becoming dangerously parochial.

The City's reawakening is part of a seismic shift in European economic, social, and political attitudes. A new equity culture is developing across Eastern and Western Europe as citizens realize

that their cash-strapped governments will no longer be able to provide for their retirements. That change will mean a surge in demand for mutual funds and other investments for City firms to create and manage. A new generation of profit-driven managers and activist shareholders, meanwhile, is demanding that European corporations improve their performances. To do so, corporations are searching for cheaper and more creative sources of financing. That means huge new quantities of equity and debt for City firms to underwrite.

Not even Britain's decision to stay out of the European Monetary Union for the next few years seems likely to hurt the City's prospects of becoming Europe's preeminent financial center. For now, bankers aren't worried about Britain's reluctance to join EMU. Maybe that view will change if, 10 or 20 years from now, Britain were still out and isolation made doing business in Europe difficult. But most bankers assume Britain will join EMU long before then.

GREAT EXPECTATIONS. In the meantime, City bankers are rubbing their hands over the prospect that European financial services may turn in hotter growth than those in the U.S. over the next two decades. Sallie L. Krawcheck, an analyst at New York's Sanford C. Bernstein & Co., estimates that with private pensions and mutual funds growing at a 30% annual clip in some European countries, the overall equities and investment banking business will grow 15% annually for the next five years. That's twice the rate of growth expected in the U.S. The financial-services industry accounts for 25% of Britain's



HUSTLE AND BUSTLE

After a long decline, London now dominates trading in currencies and international equities

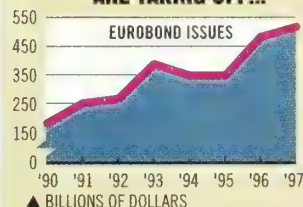
gross domestic product and employs 1 million people.

Banks are drawn to the City's fortuitous time zone, supportive regulation, and a deeply ingrained risk-taking culture. In the rush to remake the City to serve a new Europe, most of the local merchant banks that once dominated corporate finance in London have been taken over by foreign firms. The surge of international investment has improved the City's game. Indeed, it is "a great source of strength," says Bank of England Governor Eddie George, noting that the recent arrivals "bring new ideas and innovations," as well as "international connections." To be sure, the majority of City workers remain Londoners, who took home a hefty share of the \$1.6 billion in bonuses paid out last year. But proud names such as Warburg and Morgan Grenfell are

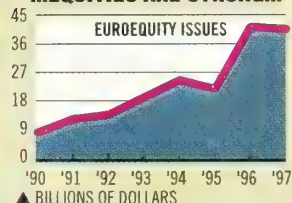
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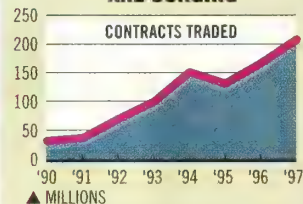
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hands. Dozens of smaller firms swallowed up by bigger fish after the 1986 event known as Big Bang. Then-Prime Minister Margaret Thatcher, Big Bang abolished minimum commissions and opened up membership in the clubby London Stock Exchange.

The invasion of foreign banks—565 now have offices in London—is just one sign of the reborn City. Since 1992, the cramped City has been rebuilt in the past two years. Eager for more space, bankers are moving into Canary Wharf, the massive estate project on the Thames. Reichmann's glass complex, which opened to receivership in 1992, is now a roaring success. A record 1.5 million square feet of office space was built out there in the last year, and the bank is putting up a new building. It isn't the first time the City has thrived on the global stage. In the 19th century, London was the undisputed center of the commercial world. Its banks made and lost fortunes financing the only trade but a global surge in international trade, including America's new rail-

roads and southern Africa's gold mines.

The City's stature declined this century as Britain lost its empire and fell into an introspective funk. But the creation of the Eurobond market in the late 1960s, as banks flocked to London to circumvent U.S. capital restrictions, started reviving the City's fortunes. The prospect of a single European currency and the current bull market in stocks, mergers, and acquisitions have helped the City regain its former clout.

Now, London dominates trading in international equities and does about \$460 billion in foreign-exchange transactions every day. City bankers lead the world in cross-border loans, with some \$1.5 trillion outstanding. The City is also a powerful force in the fast-growing derivatives industry. And many financial institutions have made London their command post for the big investments they plan for such emerging markets as Russia, Poland, Turkey, and South Africa.

Still, when financiers size up the Continent, they see even greater financial opportunity. Europe has a larger econ-

omy than the U.S., with a GDP of nearly \$9 trillion, vs. \$7.6 trillion for America. Yet outside of Britain, Europe's capital markets remain largely undeveloped. In contrast to the U.S., where corporate bonds and equities drive most company financing, Europeans are still largely restricted to borrowing from banks. In addition, most European investors are skeptical of stocks, let alone high-yield debt. The combined value of Europe's stock markets is equivalent to only 75% of its GDP, vs. 154% in the U.S.

CONTINENTAL SHIFT. The potential revenues and fees to be gained by opening up European markets are enormous. Institutional investments in Britain, Germany, France, Italy, and Spain total \$5.2 trillion now. That's equivalent to 77% of their GDP, says Bernstein's Krawcheck. America's \$13.6 trillion in institutional investments, by contrast, are equal to 189% of its GDP. If European assets under management approached anything near a similar proportion of the economy's size, an additional \$10 billion in money-management fees could roll into the City's banks. Europe's in-

Profits on Wall Street to pay for expansion abroad

creasingly important corporate debt market could produce as much as \$700 billion in new paper per year within five years, says Bill Winters, head of European fixed income at J.P. Morgan & Co. in London.

But even as they ponder these enormous sums, bankers already are making big money helping European companies merge. With more and more businesses disposing of underperforming assets and buying other companies to position themselves for EMU, the value of European mergers increased 20% last year to \$326 billion, says Securities Data Co. That's one reason the City's 1997 bonuses jumped an estimated 20% to 25%, say human resources experts.

The prospect of further rich pickings is why Goldman, Sachs & Co. put up a gleaming tower on Fleet Street, where newspaper reporters used to roam, and why Merrill is building an office block for 5,500 workers by 2001. These and other major institutions also have big offices in Frankfurt, Paris, and elsewhere on the Continent. But key executives sit in London. Says one investment banker: "When we need firepower, we put people on a plane from London."

Even the new European Central Bank's Frankfurt base is unlikely to diminish London's importance. Just as in the U.S., where monetary policy is set by the Federal Reserve Board in Washington and traded upon by banks in New York, the European money market may wind up split. "London will be the largest center for euro trading in foreign exchange, swaps, and government bonds," predicts J.P. Morgan's Winters.

Frankfurt isn't conceding defeat. Its electronic futures market now dominates trading of the German long bond contract—a position once held by the London International Financial Futures & Options Exchange. But if the euro is overregulated, the Continental traders' gains will shrink, and London will get more business. **PLAYING CATCH-UP.** Although European institutions have the advantages of long-standing client rosters and strong balance sheets, that may not be enough. The Americans boast wide access to U.S. investors, something no Europeans have. And unlike their U.S. competitors, most European banks are serious players only in their home markets. To compete in the new global economy, they'll need to make up for lost time.



For years, they were able to show minuscule returns in investment banking without drawing shareholder ire.

After the Americans stormed the City in the early '90s, Barclays Bank, Deutsche Bank, and National Westminster Bank tried to catch up to them. So far, though, it has been no contest. The only Europeans to make a splash have been SBC Warburg Dillon Read Inc., an amalgam of several institutions in Britain, Switzerland, and the U.S., and the Lazard houses. Lazard ranked second, between Morgan Stanley, Dean Witter, Discover & Co. and Goldman Sachs, in European mergers last year. "My friends thought I made a mistake," says a Briton who joined Goldman Sachs in the 1980s. "Now they all wish they were here."

Despite the competition, Merrill saw enough potential in Europe to pay \$5.3

MOVING IN
Many players
are expatriates
like Merrill's
Naomi Molson,
an M&A whiz
from Canada

when British mail-order giant General Universal Stores (GUS) hired Merrill to mount a \$2.6 billion hostile bid for catalog retailer Argos PLC.

There are some clouds on the City horizon. Monetary union will create disruption. The chaos expected from the switch from individual currency-denominated bonds to euro instruments could sharply decrease new issues. Another banking mainstay, foreign-exchange trading, is likely to crumble—although London, which dominates European dollar and yen trading, won't suffer as much.

Frankfurt and Paris, which rely heavily on European currency trading. More worrisome is that so many City-based banks have similar strategies for Europe. "If you add up the market share everybody thinks they have to gain, it probably comes up to 200% of the like business," says a skeptic banker.

All this means more competition and pricing pressure. Price-cutting has made European privatizations much less attractive to bankers. And the bear market could dry up the deals overnight and trigger layoffs. But no one's thinking bear market now. As Europe gets ready for the euro, London's dealmakers are still reaping their new golden age.

*By Stanley Reed
in London*

Why London Is Where It's At

EXPERIENCE Its place at the center of the Eurobond and equity markets has given it long experience with international securities deals.

LOCATION It offers easy access to the U.S., Europe, and key emerging markets. Its time zone between North America and Asia allows traders and bankers to call anywhere from Singapore to San Francisco during a single workday—an important plus as global investing surges.

LOW TAXES British taxes are lower than on the Continent and favor expatriates, making it easy for investment banks to set up and attract staff.

OPEN REGULATION Its regulation is flexible, transparent, and tolerant of innovation. The legal system is more protective of shareholders than Continental regimes.

LIQUIDITY With so many banks, fund managers, and corporate headquarters, London is the world's most liquid capital market outside of New York. That makes it an easy place to raise and invest money.

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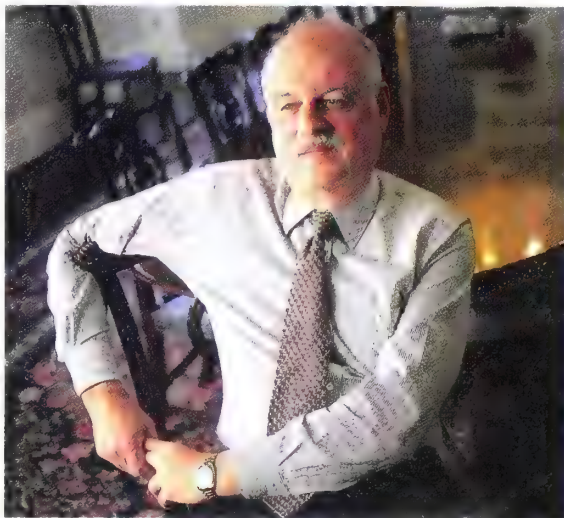
Two years ago, Aetna Inc. seemed to be on the verge of transforming the health-care landscape. It bought U.S. Healthcare Inc. for an eye-popping \$8.2 billion. Executives talked of creating the first national, fully integrated managed-health-care insurer. With the industry rapidly consolidating, Aetna would be among the handful of behemoths able to dictate terms to customers and health-care providers alike.

The rhetoric was quite different on Mar. 15, when Aetna agreed to buy New York Life Insurance Co.'s health-insurance business for \$1.05 billion. "We've redefined what we are," says Chairman Rich-

"A PAINFUL WAY TO LEARN": Huber says the U.S. Healthcare merger was messy

ard L. Huber, an international banker who joined Aetna in 1995. While Aetna is still acquiring, the insurer has abandoned ambitious plans to expand aggressively into managed care. "We're an insurance company," he says. NYLCare, which will add only 2.5 million members to Aetna's 13.7 million, lost \$30 million last year on \$3.2 billion in revenues. Last year, Aetna netted \$901 million in revenues of \$18.5 billion. **"A CRAPSHOOT."** Why the strategy shift? Melding U.S. Healthcare, a brash health-maintenance-organization operator, proved far more difficult and costly than anyone thought, and the process is not finished yet. Computer system snafus, exacerbated by overzealous staffing cuts, have alienated customers and fouled up pricing strategies. Originally, Aetna promised the merger would cut \$300 million from costs by the end of 1997, but less than half that has been realized. Says J. Randall MacDonald, senior vice-president for human resources at GTE Corp., an Aetna customer: "One plus one doesn't equal three, and I'm not even sure it equals two."

Meanwhile, the managed-care merger wave Aetna hoped to lead hasn't happened: The balance of power is shifting away from insurers toward employers, doctors, and hospitals. Indeed, while Aetna has been struggling to rationalize two



BACK TO BASICS

NOVEMBER, 1995 Having gotten out of the reinsurance and annuity businesses, Aetna sells its underperforming property-casualty division. Chairman Ronald E. Compton says the company will focus on managed health care.

APRIL, 1996 Aetna agrees to buy U.S. Healthcare for \$8.2 billion.

JULY, 1997 Doctors complain about claims payment backlogs. Big employers chafe at tough, U.S. Healthcare-style sales tactics.

DECEMBER, 1997 Richard L. Huber is named CEO of Aetna. He concedes consolidation snafus.

MARCH, 1998 Huber is named chairman. Aetna agrees to buy NYLCare for \$1.05 billion. Deal is far more conservative than U.S. Healthcare, and so is the consolidation timetable. Huber talks about Aetna reverting to being an insurer, rather than a managed-care company.

DATA: BUSINESS WEEK

strikingly disparate organizations, doctors and employers have rebelled against its attempts to apply U.S. Healthcare's aggressive pricing and controls to Aetna's sclerotic existing business.

Back in 1996, the U.S. Healthcare deal looked like a winner. But it soon became apparent that Aetna had bought at the height of a market that quickly plummeted. Consolidation of claims-processing centers and 4,950 layoffs helped reduce Aetna's overhead expenses to

19.2% of revenues last year from 22.3% in 1996. But cuts were too deep and too fast, as Huber now concedes. Corporate customers complained about problems matching employee files with data. Doctors and hospitals got testy about payment delays. Even now, getting paid properly is "crapshoot," says the office manager for one Connecticut doctor.

HIRING AGAIN. With a huge lag in claims processing, executives didn't realize until the third quarter that medical costs were running as much as 2% higher than

forecast. By then, Aetna was negotiating with 40% of its 1998 corporate contracts. Many of the resulting premiums were based on outdated cost information, so Aetna stands to see little profit on a big chunk of its business this year.

To repair the damage, Aetna has hired 550 new full- and part-time operations employees and has slowed the closing of service centers. While it has put the vast majority of its HMO members on one computer system, Aetna still plans to merge the traditional insurance operations into the system as well, a feat that has yet to be performed anywhere in the industry.

In dealing with NYLCare, Huber is taking a tight, cost-effective approach to the deal and promising much less than Aetna did with U.S. Healthcare. That seems appropriate. The only NYLCare plans that make money are the biggest ones—in Dallas, Houston, and the Washington (D.C.) area. And those won't be integrated with Aetna's computer systems for more than two years.

Huber admits that Aetna's marriage to U.S. Healthcare has been messy. "It was a painful way to learn," he admits but says he'll apply the lessons in the NYLCare merger—even if he has to sacrifice the grand vision that inspired Aetna's original expansion binge.

By Susan Jackson in Hartford

Think your corporate strategy is ironclad?



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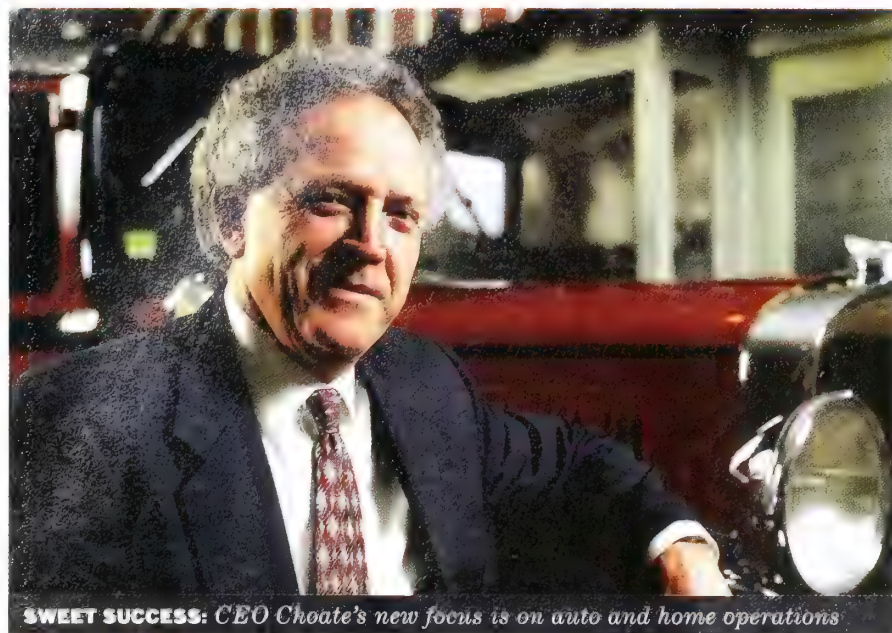
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SWEET SUCCESS: CEO Choate's new focus is on auto and home operations

INSURANCE

A TORNADO OF A TURNAROUND

Slimmer and tougher, Allstate roars back from disaster

For Allstate Chief Executive Jerry D. Choate, 1994 was a year he would rather forget. While Sears, Roebuck & Co. was planning to spin off the property/casualty insurer, Allstate was reeling from the effects of the Northridge earthquake and Hurricane Andrew, causing \$4.4 billion in losses. That forced Choate, who has just been promoted to CEO, to rein in his sales agents sharply. While the Northbrook-based insurer backpedaled, lower-cost competitors like GEICO Corp. were gaining share in Allstate's core auto insurance market. "We lost \$2.5 billion overnight," says Choate, with a note of disbelief still in his voice.

Today things couldn't be more different. Choate and Chief Operating Officer Edward M. Liddy have engineered one of the more dramatic corporate turnarounds of the '90s by re-making the company. They have sold off commercial insurance and reinsurance businesses and

focused on auto and home lines. They have battled with state regulators to reduce risk in their homeowners portfolio. And they've sharply cut costs in claims-processing. "They've done a superb job," says Harry D. Cohen, portfolio manager of the Smith Barney Appreciation Fund. Allstate, one of the BW 50, has been Cohen's largest holding for the last year.

It has also been one of his most profitable. In the past three years, the stock has more than tripled, to a recent high of 96, outperforming both the S&P 500 and the S&P property and casualty insurance index by wide margins. Allstate's profits have soared by an average of 76% in the same period. Last year, the company earned a record \$3.1 billion, on revenues of \$25 billion.



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ACCOMPLISHMENTS

- Reduced exposure to catastrophic losses
- Increased capital from \$6.5 billion to \$13 billion
- Entered new markets
- Return on equity twice industry average

CHALLENGES

- Achieving stronger top-line growth
- Maintaining price competitiveness
- Expanding life-insurance division
- Satisfying shareholders and policyholders both

For Choate, a 36-year Allstate veteran who sold insurance out of a Sears store in Denver, Colo., success is a long time coming. His first priority on taking office was damage control in the homeowner business. While making up less than 20% of Allstate's total written premium, homeowner policies were generating enormous losses from catastrophes in Florida and California.

CUTTING RISK. Solution? Get out of the business. Allstate stopped renewing thousands of policies in 1993, and eventually paid an undisclosed amount to Clarendon National Insurance Co. to take over thousands more. By laying off extra risk to reinsurers, Choate now says Allstate's maximum expected loss in Florida is less than \$1 billion.

He applied the same strategy in California, where Allstate took losses of \$1 billion from the 1994 Northridge earthquake. The state government has taken over most of the underwriting of earthquake insurance through the California Earthquake Authority, a quasi-public agency to which Allstate has contributed \$150 million so far.

Now Choate is concentrating on auto insurance, which accounts for 75% of Allstate's \$18.8 billion in property and casualty premiums. In an increasingly price-driven market, Allstate and other agent-based auto insurers, such as State Farm and Farmers Group Inc., have a serious handicap against direct marketers such as GEICO. Allstate spends about 23¢ of every dollar of premiums on agent commissions and administrative

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Average Annual Returns As Of December 31, 1997

BETTER.

AMERICAN CENTURY 5-STAR PERFORMANCE				
Average Annual Total Returns As Of December 31, 1997	1 Year	3 Years	5 Years	Life of Fund
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tive expenses. That compares with 14¢ at GEICO, which sells insurance over the telephone.

Choate, however, maintains that most Americans will continue to buy insurance through agents. So instead of developing lower-cost distribution channels, which would have his agents up in arms, Choate has concentrated on cutting the cost of claims: "Seventy-five percent of the money flows through the claims side of the business," he says. "That's where the leverage is."

PLAYING TOUGH. Choate is also in a war with trial lawyers to cut litigation expenses. The company now routinely sends letters to third parties injured in accidents with Allstate customers to try to persuade them not to hire a lawyer. In several states, lawyers have filed suit against the company for "misleading" accident victims about their rights.

Choate makes no apologies for playing tough. "We want to pay what we're liable for, no more, no less," he says. Wall Street loves that attitude, but some consumer advocates don't. "They've always played hardball on claims," says Robert Hunter, director of the Consumer Federation of America. Still, the company continues to retain more than 90% of its customers and has kept its market share of about 12%.

Allstate is increasing its share of the lucrative "nonstandard" auto market: people who have poor driving records or own exotic, expensive-to-repair cars. They incur higher losses and pay higher premiums than standard customers. The \$18 billion market has been the No. 1 source of growth for Allstate in the last five years. With a 17% market share, Allstate has surpassed Progressive Corp. as the segment's largest player.

Choate is also targeting inner cities for home and auto insurance, a \$25 billion market. For years, housing advocates such as Shanna Smith with National Fair Housing Alliance have accused Allstate and other major insurers of redlining neighborhoods. Now Smith is tentatively praising Allstate.

Many insurers don't want the hassle of trying to figure out how to price policies for difficult risks. But Rhonda Woodard, vice-president of underwriting at Allstate, says there are good opportunities for companies "that have figured out there's more to the cities than what appears on the six o'clock news."

In an industry growing at 3%, Allstate needs all the opportunities it can get. But given the way it has taken to flying solo, the revitalized insurer has a very good shot at maintaining the momentum.

By Andrew Osterland in Chicago

BANKING

BIGFOOT HEADS SOUTH

Washington Mutual goes after Wells Fargo and BofA

Back home in the Seattle suburb of Bellevue, Kerry K. Killinger takes great pride in how fast he can mow his 5,000-square-foot backyard. His best time, says his wife Debbie, is seven minutes. It's little wonder then that the 48-year-old chairman and CEO of Washington Mutual Inc., which towers over its thrift rivals, has taken such apparent glee in cutting a swath through West Coast banking. His latest move, the \$9.9 billion acquisition of H. F. Ahmanson and its giant Home Savings of America, should put California behemoths Bank of America and Wells Fargo on alert for Killinger's combine.

Over the past seven years, using Washington Mutual's rocketing stock, Killinger has transformed an obscure \$8 billion-in-assets thrift into the first institution with the breadth to challenge BofA and Wells Fargo in California's fragmented retail banking industry. Since 1996, Washington Mutual will have paid \$20 billion in stock for such major California savings-and-loan players as American Savings Bank, Great Western Financial, and now, Home Savings. That has given it \$150 billion in assets, vs. Wells Fargo's \$100 billion and BofA's \$260 billion. "Before, you had two seven-foot, two-inch giants and a bunch of junior high school kids on the court," says Lehman Brothers Inc.'s Philip R. Erlanger, Washington Mutual's lead investment banker. "Now, you have another power forward in the game."

The thrift's main game is mortgage lending. With Home Savings, it will be the West Coast's biggest, with almost twice as many loans as No. 2 BofA. Mort-

gage banking has been a notoriously unrewarding business. But no one has done a better job of using technology to lower the cost of loan origination and enticing customers to try other services, such as checking accounts and home equity loans, says Salomon Smith Barney analyst Thomas O'Donnell.

Washington Mutual doesn't compete in many commercial arenas, such as midsize corporate loans, but it has been moving in on many consumer businesses—such commercial banks as Wells and BofA. Washington Mutual is bringing 23,000 new households each month, lured by the thrift's promise of totally free checking—something commercial banks largely resist. And those free accounts, which lower funding costs, have given

a heady source of fee income. The thrift charges a steep \$3 penalty for bounced checks, helping it earn an average \$200 in fees annual-

KILLINGER: The plan includes better service and a focus on consumer banking

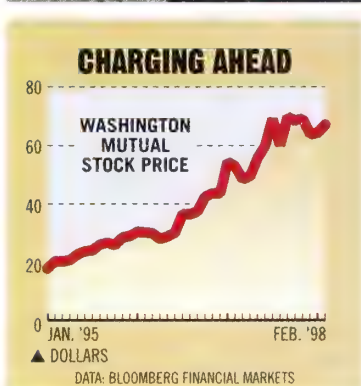
from each account. "We're now every bit as strong as Bank of America and Wells," says Killinger.

His southern march comes at a bad time for Wells, which has had trouble consolidating its 1996 purchase of First Interstate. It has lost more customers than it intended to during its cutback of branches. Although BofA may have gained overall, it has lost its No. 1 position in mortgage lending.

Killinger's move is

not without challenges. His commercial bank rivals enjoy big advantages, including a more robust automatic-teller machine network, an extensive branch network in supermarkets, and a greater breadth of consumer products. Killinger claims his network of some 700 branches in California will compensate with better service, competitive prices, and a strict focus on consumer banking. It's not a novel approach, but it's one that has served the lawn man from the north well so far.

By Kathleen Morris in Los Angeles



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BY GENE G. MARCIAL

ICAHN MAY HELP SEAGULL FLY

One victim of sliding oil prices is Seagull Energy (SGO), an independent international oil-and-gas explorer and producer. Its stock, up as high as 27 in October, is down to 16. But that's just dandy for financier Carl Icahn, who is rumored to be methodically snapping up shares: Whispers are he has accumulated some 1 million.

Icahn's interest in Seagull had been talked about even before he made known his intention in early March to rescue Pan Am from bankruptcy. He has since abandoned that plan. But not his appetite for Seagull, according to an Icahn associate. Icahn has filed with the government his intention to acquire at least a 15% stake in Seagull.



CARL ICAHN:

Exploring the oil business again?

That prompted the company to revise its poison pill to enable Seagull shareholders to buy shares at half the price of the stock once any investor acquires a 10% stake. But Icahn is not daunted by any poison pill, says the associate. "Seagull needs to be acquired by another group and then restructured to enhance shareholder value," he says. He notes that management owns only a negligible number of shares. "There are many ways to skin a poison pill, and Carl is an expert at them," he adds.

This pro believes that Seagull has been approached by another group for a friendly deal, but he says that management turned it down. At its current price, "there's no risk involved" in buying in, he says, with the stock trading at just four times its cash flow and selling for just half the value of its total assets. He thinks that Seagull is worth 23 at current oil prices. But if prices rebound, it's worth 30, he adds. Seagull explores for and produces oil and gas mainly in the U.S., Egypt, Indonesia, and Tatarstan, a member of the Russian federation. Revenues were \$549 million in 1997. Seagull is expect-

ed to earn 50¢ a share this year and 59¢ in 1999, down from 1997's 77¢.

Seagull Chairman and Chief Executive Barry J. Galt says that Icahn has not communicated with the company. He declined comment on whether Seagull has been approached by another group. Icahn didn't return calls.

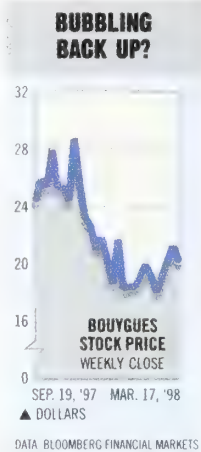
BOUYGUES COULD BE A GUSHER

Ever heard of Bouygues Offshore (BWG)? Not only is it a French company little-known in the U.S., it's also in the currently out-of-favor oil business. But Bouygues (pronounced "bweeg"), which trades on the Big Board, has attracted some savvy U.S. market players—even as many big investors have bailed out of oil-related stocks. One believer: money manager David Marcus at Franklin Mutual Advisers, which has acquired a 7% stake. "We're a value-driven, contrarian investor who looks for undervalued companies whose shares have been thrashed by investors for one reason or another," Marcus says. Bouygues, which traded as high as 29 a share in November, is currently trading at 20.

"Bouygues is a compelling buy because it's a play on tomorrow in the oil industry," says Marcus. He notes that Bouygues, an international contractor that builds onshore as well as floating deepwater oil platforms, has been signing off on many new projects.

Recent deals include a \$69 million joint venture in Congo to supply Elf Congo with two platforms, pipelines, and electrical cables. It also signed three contracts to install pipelines in the Gulf of Mexico. Bouygues Chairman Ivan Replumaz is optimistic that contracts for a \$300 million deal in Angola, a \$100 million pact with Exxon in Chad, and an \$80 million project with Mobil in Nigeria, will be won this year.

Analyst Jeffrey Freedman of Prudential Securities says contract awards in 1998 will translate directly into solid earnings in 1999. He expects Bouygues



to earn \$1.10 a share in 1998 and \$1.4 in 1999, vs. 1997's 96¢.

DOES RESPONSE HAVE THE ANSWER?

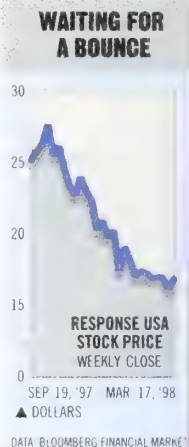
Response USA (RSPN) would appear to be in a win-win situation: This provider of integrated electronic security for homes and small businesses is in an industry that's rapidly growing—and where the big players are rushing to consolidate. Yet shares of Response, the 18th-largest in the business, have been acting like losers. They've slumped to 5¢ on Mar. 17 from 11 in mid-October. What's weighing Response down?

In part, the stock is weak because of a secondary offering of 3 million shares at 6¢ on Feb. 5, which more than doubled the shares outstanding. Still, some big investors have bought stock. Among them are Mario Gabelli, who bought some 300,000 shares for the Gabelli mutual funds, and New York hedge fund Gabriel Capital, which acquired some 150,000.

Response services some 60,000 residential and small-business subscribers in New York, Connecticut, New Jersey, Pennsylvania, and Delaware, and is one of the few independents left in the electronic protection business. In July, 1997, Tyco International acquired ADT, North America's leading provider of electronic security services. And Western Resources in November bought 82% of Protection One, which provides monitored security services in seven states.

Before the stock offering, Protection One's investment banker had sent feelers to Response seeking to buy privately all the 3 million share offer at 7 apiece. President and CEO Richard Brook who turned down the offer, says: "In a couple of years, we will grow large and command a much higher price."

Gruntal analyst Mark Langley expects earnings before interest, tax, depreciation, and amortization of 70¢ in 1998 and 92¢ in 1999. He thinks the stock will hit 9¢ in a year.



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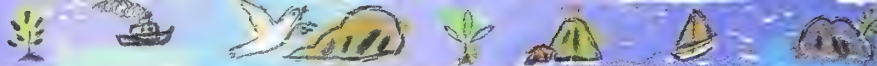
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EDITED BY AMY DUNKIN

Georgia Isles On My Mind

My wife's oldest friend, a Manhattan native and cosmopolite who has lived in Atlanta these past dozen years, once warned me about travels in Georgia. "Prepare to be disappointed," she said. Her

words were on my mind recently as we turned off Interstate 95 at Route 17 and headed east toward Jekyll Island, a path that leads first past Ga. Pig Barbecue, over Fancy Bluff Creek, and across the Marshes of Glynn, a soggy tract that was celebrated by the 19th century poet Sidney Lanier but today lies next to smelly pulp mills.

A century ago, after J.P. Morgan and a few dozen other tycoons bought Jekyll and began wintering together there, no one arrived this way. Morgan

came by *Corsair*, his yacht, and others by ferry after taking a train to nearby Brunswick. They formed the Jekyll Island Club, a Gilded Era version of the Sun Valley (Idaho) retreats financier Herbert Allen now puts on each summer for Bill Gates,

Michael Eisner, and other corporate leaders of today's Digital Era. One winter, Jekyll club members sat around and drew up plans for what became the Federal Reserve. A few years later, AT&T President Theodore Vail placed the first transcontinental call from the island.

Abandoned during World War II by its wealthy patrons, Jekyll since 1947 has been owned by the state of Georgia. Now, if you persist along Route 17 to its intersection with Route 520, take that to the toll booth, and pay \$2, you will find yourself amid the most curious combination of nature and society in

the barrier group known here as the Golden Isles. Despite my friend's warning, I was far from disappointed.

You may have become aware of this part of the world a couple of years back when John F. Kennedy Jr. married on nearby Cumberland Island, which guards Georgia's southernmost flank

and once was owned by Andrew Carnegie. It's famously remote: Accessible only by ferry, it offers some National Seashore campsites (912 882-4335) or 15 rooms at Greyfield Inn (904 261-6408).

RITZY ENCLAVE. North of Cumberland lies Jekyll, and north of Jekyll is St. Simons Island, which is another scene altogether. With busy boutiques, dining districts, art galleries, and plentiful weekly rentals, St. Simons is to Atlanta as the Hamptons are to New York City. Still further, hugging the northern shore of St. Simons, are two smaller islands. By car, you can reach Sea Island, an enclave of luxurious homes that lured the likes of Coca-Cola's late chief, Roberto Goizueta, and which boasts an equally luxe hotel, The Cloister (912 638-3611). Another ferry trip beyond that is Little St. Simons, a private, undeveloped territory with no cars and just one hotel, the Lodge at Little St. Simons Island (888

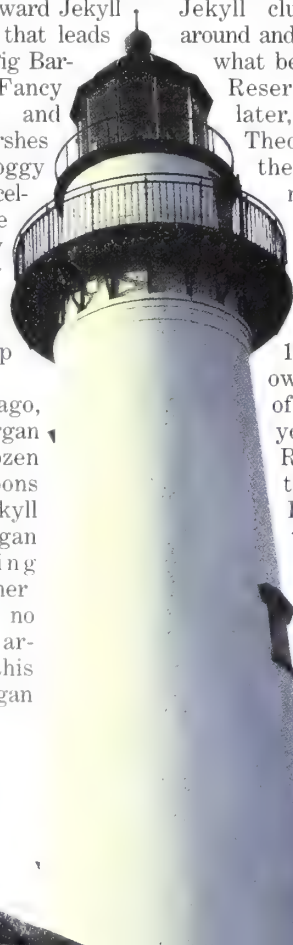
733-5774). It offers canoeing, horseback riding, and outfitting with staff naturalists.

Each of the Golden Isles has obvious appeal, but the virtue of its history, Jekyll a place apart. Called Ospo to the natives, the island was invaded by the Spanish in 1566. They gave way years later to the British, who renamed it Jekyll after one of Georgia founder James Oglethorpe's British sponsors. Some 9 miles long by 1 mile wide, it faces the Atlantic with a long, broad beach. It has dunes, grasslands, and most striking forests of pine, palms, and dramatic oaks, twisted by the wind into bonsai-like shapes.

This is the landscape that J.P. Morgan & Co. found appealing enough to pay \$125,000 for in 1886. Amid the oaks on the leeward side, they first built a huge common building, a rambling Victorian. Today, the Jekyll Island Club Hotel (800 535-9547), it's the island's main accommodation, a

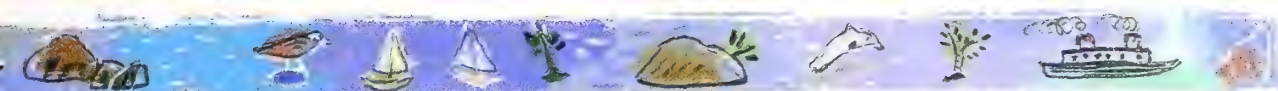


Island Travel
GOLDEN ISLES



**A BEACON
FOR TOURISTS:**
The lighthouse at
St. Simons
Island





SCENIC PASS: Jekyll Island's oaks are sculpted by the sea breezes. The island's north end offers horseback riding

several familiar chain
jostle along the beach,
ves as a hub. Check out
oar's head, with its pink
e jutting out, that peers
the dining room from
the drawing-room man-
n spring and summer,
d rates for a double
run from \$119 to \$259 a
veral club members,
s and Goodyears among

them, went on to build what
they called "cottages," which
were in fact lavishly fur-
nished dormitories three sto-
ries tall. Many have been
renovated, and walking tours
are offered daily. My dream
house is the coral-colored Vila
Marianna: 15 rooms, six
baths, plus a bell tower ter-
race with view.

The best way to see the
island, more than two-thirds

of which remains untouched
despite 63 holes of golf, is by
bike. Our 15-mile tour of
Jekyll took us along the is-
land's marshy west side,
where the trail takes wind-
ing turns beneath canopies of
moss-draped oaks, past an old
plantation graveyard, and by
ruins of "tabby," the indige-
nous building material of
sand, lime, and oyster shell.
Traveling amid these sights,
and listening to the birds and
the wind in the grass, you
might think this is paradise—
until the northwest breeze ar-
rives, carrying an odor from
the pulp mills that only a
timber executive could love.
Seeing the marsh, I also
imagined how large the mos-
quitoes might grow by sum-
mer, and learned later that

sand gnats, too, bedevil visi-
tors in spring and fall.

Pedaling on, at Jekyll's
north end we headed toward
a fishing pier at Clam Creek
Picnic Area (which offers
horseback riding) and gazed
across the harbor's mouth to-
ward St. Simons and its light-
house. Rounding Jekyll to its
east side, we found the At-
lantic, which had been laid
flat by a stiff offshore wind
and now lapped gently along
miles of broad, sandy beach.
As we headed south, the trail
edged further inland, skirt-
ing first the beach hotels and
then a ridge of dunes where
shade was hard to find. Next
was a boardwalk named Glo-
ry, after the Civil War-era
movie filmed there a few
years back. Here, the ele-
ments seem to have beaten
the vegetation down to small-
er varieties—wax myrtles,
cypresses, and sea oats—and
traversing the isolated dunes
via the boardwalk toward the
ocean grew spooky.

As we swung around the
island's narrow south end, the
bike trail ended at St. An-
drews Picnic Area, which
faces west and looked like a
good spot to catch the sunset.
It was just past lunchtime,
though, so we headed back
toward the island's marina
and a restaurant there.

VICTORIAN TEA. Sitting on a
deck beneath the green-and-
white awning, I looked out
and saw the Rhumba, a
yacht from Wilmington, Del.,
and learned that some people
still arrive at Jekyll by boat
along the Intracoastal Wa-
terway. Others fly in to the
3,700-foot airstrip, sometimes
just for lunch or the Victori-
an tea served daily at 4 p.m.
at the Jekyll Island Club
Hotel. Most people now
drive here, of course, some
after flying by commuter
plane to Brunswick, about 20
minutes away, or by bigger
jets to Jacksonville, Fla., 60
miles south on I-95. Few
people, I imagine, depart
disappointed. *Robert Barker*

SONAL PICK: Sea Jay's Waterfront Cafe & Pub at the Jekyll Harbor Marina offers a nice view of
waterway and marshes beyond, as well as Brunswick Stew, a tasty dish of pork, beans, and corn



Eagles Overhead, Whales Below

Rarely can you report that the best part of your wonderful, three-day island getaway came during the trip home. But on my ferry ride back to the mainland from Washington's San Juan Islands in February, I had one of those "it doesn't get better than this" moments. Before me towered the awesome snow-capped bulk of 11,000-foot Mt. Baker; to the south stood the sawtooth peaks of the

OUT THERE: The isolation keeps commuters at bay

Olympic range. And all around, the sea and sky were clear and bright blue.

Such are the simple pleasures of a trip to the San Juans. This group of over 120 rock- and fir-covered islands is less than 100 miles northwest of Seattle as the eagle flies, but it's far removed from the city's vicious traffic jams and the grinding pace kept by the region's many software programmers.

How do the San Juans remain unspoiled? It simply takes too long to get there for the isles to be attractive to commuters or weekenders. There's an hourlong car ride

from Seattle to the ferry dock in Anacortes, a one- to three-hour wait (or more in the summer) to get on the boat, and then a 1½ hour trip to San Juan Island's Friday Harbor. (For schedules, call 206 464-6400 or visit

www.wsdot.wa.gov/ferries/schedules/current).

Don't let the Northwest's reputation for ceaseless rain scare you off. The islands sit in a "rain shadow" created by the Olympic Peninsula, so the sun shines an average of 247 days a year. No wonder this archipelago is hog heaven for hikers, bikers, kayakers, and birders.

Hog is an apt word when speaking of the San Juans because of a quirky bit of their history: the Pig War of 1859. Britain and the U.S. were contesting ownership of the islands and almost came to blows after an Englishman's pig was shot for rooting in a Yankee's potato patch. Two national parks on San Juan Island, American Camp and English Camp, are sites of former military garrisons and offer some gorgeous strolls.

You have to look seaward for the No. 1 tourist attraction—orcas, the black-and-white killer whales made famous by the *Free Willy* films. Nearly 100 orcas ply the waters, munching on salmon and the occasional seal. They can be spotted year-round but are most evident in the spring. Former Friday Harbor Mayor Bill LaPorte, who lives on a powerboat, recalls when a pod of orcas came so close he touched one. It shocked him by blowing spray out of its breathing hole and soaking him to the skin. Learn more about orcas at the Whale Museum in Friday Harbor.

The other star animal at-

traction is the bald eagle. About 90 nesting pairs have been counted, and I spotted two eagles in a single afternoon. Farhad Jhathan, proprietor of Harrison House Suites in Friday Harbor, says eagle sightings are commonplace: "The other day, a bald eagle flew right over my head holding a dead seagull in its talons while being chased by another seagull," he says.

DELICACIES. It's bird-eat-bird on the San Juans. But the raptors have nothing on the humans when it comes to variety and quality of cuisine. LaPorte complains that there are too many gourmet eateries, and the only time you can get a good corn dog at the San Juan County Fair is in July. But for fans of delicacies such as black-bean-and-garlic mussels, this is ground zero. Stephanie Irving, editor of *Northwest Best Places* (Sasquatch Books; \$19.95) recommends the Friday Harbor House on San Juan Island and the Bay Cafe on Lopez Island.

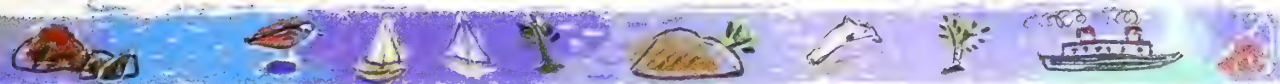
While San Juan Island is tourist central—it boasts fewer than 15 bed-and-breakfasts—other islands are also worth visiting. (Contact the San Juan Island Chamber of Commerce at 360 378-5200 or www.sanjuanisland.org.) Lopez Island features rolling hills great for biking. At the summit of Orcas Island's Mt. Constitution, easily reached by car, offers a striking view stretching from Vancouver to Seattle. No matter where you go, though, you're bound to see something that will take your breath away. *Steve Har*



BALD IS BEAUTIFUL: Eagle sightings are commonplace



PERSONAL PICK: See if you can find a flock of about 30 graceful (and sometimes noisy) trumpeter swans that frequently come to San Juan Island. Hint: Look for the road that is named after them



NEAR PHUKET: Tourists sail to James Bond Island

Asia's Islands on The Cheap

Imagine this scene: You're lying on a beach chair on Thailand's island of Koh Phi Phi, sipping a cool drink and gazing into the horizon as the sun dips into the Andaman Sea. A light breeze blows through the coconuts and cools your sunburned skin. Really? If those thoughts are compelling enough, consider this: Such a day in a tropical paradise can be had for at least 40% less than it cost last year.

With the huge currency devaluations that have swept through the region since July, vacationing on an Asian island has gotten so affordable you almost can't afford to miss it up. Southeast Asia's prime island destination—Phuket (pronounced "PHUKET") in Thailand,

Penang in Malaysia, Cebu in the Philippines, and Bali in Indonesia—all cost far less now that those countries' currencies have plunged against the U.S. dollar.

Getting there is cheaper, too. Some Asian airlines, keen to generate traffic in these tough economic

times, are offering special deals. Cathay Pacific Airways' incredible \$899 Internet All Asia Pass, for example, allows you to travel from New York or Los Angeles and make unlimited trips between 18 Asian cities—including Bali, Cebu, Penang, and Bangkok. Rarely do round-trip fares to Asia drop below \$1,000—and never do they include so many additional legs. You can reserve a ticket through Cathay's Web site, www.cathay-usa.com.

While the great seafood and souvenirs of Asia's islands are that much less ex-

pensive, the biggest savings are on hotels. One key to getting a good deal is to look for locally owned chains, as well as smaller family-run hotels. Many of the big international chains fixed their rates in U.S. dollars shortly after the region's currencies started fluctuating last year, meaning prices didn't drop as exchange rates fell. But for the most part, locally owned hotels have kept prices in the native currency.

On Phuket, which has direct flights from Tokyo, Taipei, and Singapore, there are fantastic buys. "Everything is

EASY CRUISING: Currency woes make the region a bargain

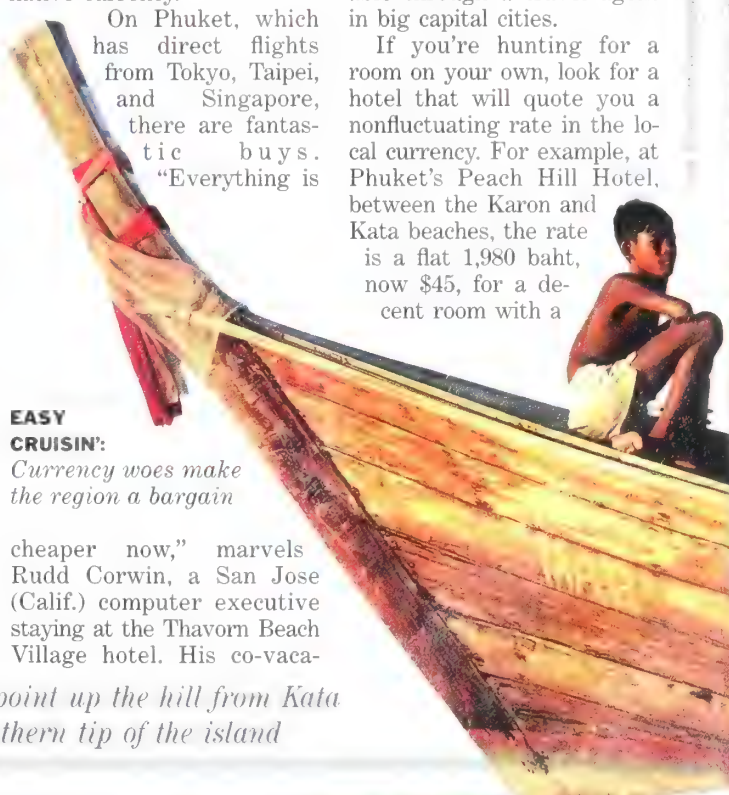
cheaper now," marvels Rudd Corwin, a San Jose (Calif.) computer executive staying at the Thavorn Beach Village hotel. His co-vaca-

tioners were quite pleased with their exchange rate of 45 Thai baht to the dollar in early March, compared with 25 just a year ago.

The hotel, a short drive north of Phuket's main Patong beach, has charged 4,500 baht for a deluxe, ocean view hillside villa since it opened last year. But with the currency depreciation, the converted price has plunged from \$180 to about \$100. At the hotel, one of four in Phuket run by the family-owned Thavorn Group, guests stay in houselike villas with wooden floors and traditional teak furniture, a plus for travelers looking for a more authentic experience.

One key to getting these great rates is to book through a local travel agent in the country you're traveling to. Even the Thavorn hotels have rates listed in U.S. dollars for people who call up and inquire in English. If you do that, the deluxe room suddenly runs \$190. But any reputable hotel will have a cheaper contract rate available through a travel agent in big capital cities.

If you're hunting for a room on your own, look for a hotel that will quote you a nonfluctuating rate in the local currency. For example, at Phuket's Peach Hill Hotel, between the Karon and Kata beaches, the rate is a flat 1,980 baht, now \$45, for a decent room with a



PERSONAL PICK: See the sunset from the lookout point up the hill from Kata Beach, or the Phromthep Cape Restaurant at the southern tip of the island



balcony overlooking the pool. Last year, that baht price would have converted to \$79. By contrast, a nearby boutique resort called The Boathouse will charge the baht equivalent of \$105 per night.

If you can say you live in the country, are paid in the local currency—or do the asking in the local language—many hotels will offer an even better rate. For exam-

ple, Thailand's Central Group, which owns hotels as well as the country's largest department store, charges \$143 per night at its colonial-style luxury resort in Koh Samui, Thailand's second-most-popular island destination. But residents of Thailand can have that same room for \$82. Also, asking for a corporate rate can result in a 20% discount.

Another way to find sav-

ings is to fly the national airline from the capital to an island destination—Malaysian Airlines to Penang, Philippine Airlines to Cebu, Thai International Airways to Phuket, or Garuda Indonesia to Bali. These carriers have not significantly raised prices, and tickets purchased through local travel agents usually will result in cheap fares. Thai Airways has kept the Bangkok-Phuket round-trip

fare at 4,000 baht, so what was once a \$160 ticket now costs \$91.

If all these bargains don't melt away your stress, try a Thai massage. In Phuket, the parlor at the foot of the Peach Hill Hotel charges the equivalent of \$4.50 for one hour of vigorous muscle rubbing, down from \$8 last year. That's almost reason enough to take an island vacation in Asia this year. *Sheri Prasse*



Bali Low— Crafts For A Song

Bali can't match Hawaii's tropical beaches, reefs, and sunsets. But as a cultural paradise, Bali is unparalleled. Balinese kids learn to carve, paint, and dance before they learn to read.

Each village in this Hindu enclave in Muslim Indonesia specializes in an artistic discipline, from wood carving to batik. Now, with the rupiah devalued by 80% since the onset of the Asian financial crisis last year, Balinese art is ridiculously affordable. Batik baby outfits sell for \$1, while elaborately carved hibiscus

wood statues go for \$10 to \$50. "Everything is so cheap, you almost feel as if you're stealing," says Doveen Schecter, an expatriate American living in Hong Kong.

The best way to shop for crafts is to head for the main road and rent a car with a driver to take you around

the island for \$15 to \$30. When you hit a village in search of handicrafts, your driver probably will steer you toward the biggest tourist trap. It usually will take credit cards and quote high prices in U.S. dollars. For the best buys, simply walk around the village, going from shop to shop. I look for

COLORFUL: One village is renowned for its carvings

family-run outlets, where artists are busy at work and children at play. Many times, their homes and workshops are behind the shops, and you can simply wander through, watching as crafts workers do their magic.

One of my favorite towns is Batubulan, known for stone carvings. Here you can find shops surrounded by sandstone Hindu deities, which the Balinese use to guard their shrines. According to Ni Gst A Oka Ariana, an employee at Yuliani, a shop packed with captivating sculptures, it takes 4 to 12 days to carve a piece. A 50-pound, three-foot statue of a lovely Balinese woman costs \$35. If you want to ship it home, add 200% to the cost. But even the shipping price is negotiable.

Head to a town called Mas for wood carvings and masks. Near the main tourist store, I found a tiny shop run by a carver and his wife. I liked the shopkeeper so much that I wanted to buy something from him, so I chose a detailed carving of the godly Hindu couple Rama and Sita for \$50.

Of all the artistic places in Bali, Ubud is nirvana. Stop at any of the museums or galleries to get a sense of the best painters. But beware: Gallery prices are massively inflated. One salesman asked

\$3,500 for a work by a local painter—and eventually settled for \$400. Many landscape paintings, made with painstaking detail, sell for less than \$100—half of what they cost when I first went to Bali in 1993.

One section of Ubud is known for its mobiles. Brightly painted wooden stars, tigers, and fish dangle from street-side stalls and sell for less than \$2 apiece. For \$2.50 you can get your hands on a stool painted with fanciful planets or animals. In another section near Monkey Forest Road, vendors offer batik quilts—the most expensive goes for \$25 and is big enough for a queen-size bed. For \$5, you can get a cotton sack for your quilt.

Other towns specialize in gold and silver, or beaded bags and belts. So be sure to pack light. Otherwise, you'll find yourself buying plenty of those \$5 bags for all your treasures. *Joyce Barnathan*

SET IN STONE: Batubulan specializes in fine sculpture



PERSONAL PICK If you see a piece of art that you like, try to track down the artist at home. You'll be able to see his latest works and bargain for a good price



(smooth operators)



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A Rustic Artists' Haven

Riding the Laura B mailboat to Monhegan Island, Me., is like taking a trip back in time. The converted Army transport, built in 1943, carries food and supplies on its front deck, and on chilly days, passengers in the stern cabin are warmed by a wood stove. In just over an hour, the Laura B makes the 10-mile trip from the fishing village of Port Clyde to one of Maine's most remarkable island treasures.

For more than 100 years, Monhegan has been a haven for artists, writers, and fishermen. Jamie Wyeth calls it his summer home. Robert Henri, Rockwell Kent, and Edward Hopper painted there, as did George Bellows, whose painting of the island's Blackhead cliff was sold at a

Maine auction last year for \$277,500.

Monhegan's sheer beauty and charming, yesteryear atmosphere make for an enchanting vacation. It's a magnet for summer tourists. Four boats from three ports ferry hundreds of day-trippers and overnight guests each

day from June through September. At peak season in July and August, nearly every hotel room is booked. Lodgings on Monhegan are simple, if not rustic. Most island rooms have shared baths, no televisions, and access to one public phone on the premises.

Barely more than one square mile, the island rises out of the Atlantic like a beached whale. Menacing 200-foot cliffs front the ocean and slope down to a flat tail near a small harbor. There are no paved roads. Only a few lo-

cally owned pickup trucks are allowed on the island. The year-round population of about 70, mostly lobstermen and their families, swells to 500 in the summer.

About 100 houses are clustered on the mainland side of the island, along with one store, five restaurants, six hotels, and a dozen or so artists' studios that are open to the public in the summer. A museum in the lighthouse—open July through September—is the main cultural attraction and holds a collection of historical artifacts. Captain John Smith, of Pocahontas fame, is said to have visited the island in 1614, and there are tales that Norsemen discovered it around 1000 A.D.

SHIPWRECK. Hiking is by necessity a popular activity. Outside the main village, the island consists of spruce and fir forests, scrubland, and moss, all pounded by the sea wind. The only access to outlying areas is by foot on 17 miles of moderately rugged trails. These take you to the cliffs and to rocky Lobster Cove, where sit the remains of the shipwrecked coal barge D.T. Sheridan. One hiking trail leads you through the

DAY TRIP: Monhegan is just 10 miles from the mainland

Cathedral Woods, an ethereal cluster of tall, mossy spruce trees, under which children like to build tiny "fairy houses" from twigs, bark, and leaves.

Birders flock to Monhegan in the spring and fall because it's on the Atlantic flyway and 100 or more species can be seen. Bring your *Peter's* guide and binoculars. The Audubon Society has an organized trip to Monhegan for members on Memorial Day weekend. Call 207 781-2330 for information.

Among places to stay, the Island Inn (207 596-0371) and the Monhegan House (207 594-7983) are the two largest hotels. One inn, the Trailing Yew (207 596-0440), has no heat and limited electricity. Shining Sails (207 596-0041) offers efficiency apartment year-round. Most hotels don't open until May 23. Room rates for two range from \$50 to \$125. Most hotels offer some dining, but it's best to inquire about the availability of food when making reservations.

Access to Monhegan is by boat from three harbors. The Laura B out of Port Clyde is the preferred mode of transportation among islanders because it is closest to Monhegan and leaves the most frequently. A round-trip ticket costs \$25, and reservations are advised (207 378-8848). Other ferry operators are Balmy Days Cruises out of Boothbay Harbor (\$26, 207 633-2284) and Harbortown Boat Cruises out of New Harbor (\$26, 207 677-2021). For information on the island's local affairs, check out www.monhegan.com.

Remember to pack light, wear sturdy shoes—and if you get seasick easily, be sure to bring along some pills. The seas can get choppy under those changeable Maine skies. *Geoffrey Smith*

PERSONAL PICK: To find out what's happening on Monhegan, stop by the shack near the general store. Look post announcements about gallery hours, boat tours, readings, history lectures, and other island events.

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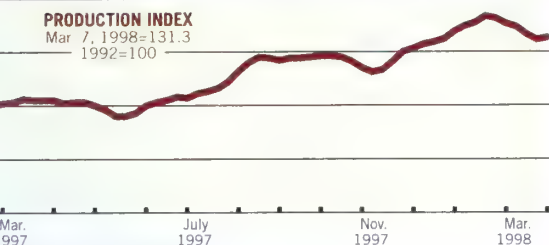
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Business Week Index

PRODUCTION INDEX

Change from last week: 0.2%
Change from last year: 4.8%



Production index rose in the week ended Mar. 7, after three weeks of decline. Before calculation of the four-week moving average, the index was up 31.6, from 130.3 a week ago. Thanks to sharp increases in loadings of motor vehicles, and metals, seasonally adjusted rail-freight traffic was up. Production of crude oil also posted a sharp increase of 6.5%, and electric as up 3.7%. Output of lumber was down 3.7%, and steel dropped 1.8%.

Production index copyright 1998 by The McGraw-Hill Companies

PRICING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
PRICES (3/13) S&P 500	1068.59	1055.69	34.7
RATE BOND YIELD, Aaa (3/13)	6.69%	6.81%	-11.0
TRIAL MATERIALS PRICES (3/13)	NA	NA	NA
SUPPLY, M2 (3/2) billions	\$4,116.3	\$4,106.6r	6.6
CLAIMS, UNEMPLOYMENT (3/7) thous.	298	305r	-3.6
AGE APPLICATIONS, PURCHASE (3/13)	217.2	221.1	14.9
AGE APPLICATIONS, REFINANCE (3/13)	1,337.9	1,403.4	221.5

Sources: Standard & Poor's, Moody's, *Journal of Commerce* (Index: 1990=100), Reserve, Labor Dept., Mortgage Bankers Assn. (Index: March 16, 1990=100)

INTEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
AL FUNDS (3/17)	5.47%	5.44%	5.42%
COMMERCIAL PAPER (3/17) 3-month	5.47	5.49	5.53
CERTIFICATES OF DEPOSIT (3/18) 3-month	5.58	5.58	5.52
MORTGAGE (3/13) 30-year	7.22	7.28	7.98
FIXED RATE MORTGAGE (3/13) one-year	5.86	5.78	5.86
LIBOR (3/13)	8.50	8.50	8.25

Sources: Federal Reserve, HSH Associates, Bloomberg Financial Markets

Data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

DUABLE GOODS ORDERS

Friday, Mar. 25, 8:30 a.m. EST ▶ New orders for durable goods manufacturing increased by 0.7% in February, above the median forecast of economists surveyed by Standard & Poor's MMS, one of The McGraw-Hill Companies. Orders had risen in January, but that followed a 5.3% drop in December, caused mostly by a drop in demand for aircraft. The increase in orders suggests that the backlog of orders also rose.

NEW HOME SALES

Friday, Mar. 25, 10 a.m. EST ▶ Existing home sales probably sold at an annual rate of 1.1 million in February, the same high

rate as in January. If so, home resales in the first quarter are running well above the sales rate of the fourth quarter, suggesting that household purchases of furniture, electronics, and textiles will increase in coming months. Unseasonably mild weather in parts of the country, coupled with low mortgage rates, buoyed home buying.

UNEMPLOYMENT CLAIMS

Thursday, Mar. 26, 8:30 a.m. EST ▶ New filings for state unemployment benefits likely stood at 320,000 in the week ended Mar. 21. Claims slipped below the 300,000 mark in the first week of March, to the lowest level since July, 1997. The jobless rate dipped to a 24-year low of 4.6% in Febru-

ary, and the drop in claims suggests that labor markets tightened further in March.

PERSONAL INCOME

Friday, Mar. 27, 8:30 a.m. EST ▶ Personal income likely increased another 0.5% in February, on top of the 0.6% gain posted in January. That's indicated by the strong advance in jobs and wages for the month. Consumer spending likely rose 0.5% in February. In addition, the revision to January retail sales, from a 0.1% increase to a 1% jump, suggests that the 0.4% gain in January consumer spending will also be revised higher. Real consumer spending is on track to grow at an annual rate of about 5% in the first quarter.

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (3/14) thous. of net tons	2,102	2,216#	-0.2
AUTOS (3/14) units	120,080	109,167r#	-5.2
TRUCKS (3/14) units	141,860	149,784r#	1.7
ELECTRIC POWER (3/14) millions of kilowatt-hrs.	64,390	61,959#	8.4
CRUDE-OIL REFINING (3/14) thous. of bbl./day	14,581	14,548#	6.3
COAL (3/7) thous. of net tons	22,916#	20,065	8.8
LUMBER (3/7) millions of ft.	477.8#	494.7	-6.4
RAIL FREIGHT (3/7) billions of ton-miles	27.5#	26.5	3.8

Sources: American Iron & Steel Institute, *Ward's Automotive Reports*, Edison Electric Institute, American Petroleum Institute, Energy Dept., WWPAl, SFPaZ, Association of American Railroads

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (3/18) \$/troy oz.	290.400	294.100	-16.8
STEEL SCRAP (3/10) #1 heavy, \$/ton	135.50	135.50	-0.7
COPPER (3/13) ¢/lb.	84.1	81.8	-28.1
ALUMINUM (3/13) ¢/lb.	69.5	70.0	-13.7
COTTON (3/14) strict low middling 1-1/16 in., ¢/lb.	64.42	66.10	-11.4
OIL (3/17) \$/bbl.	12.99	14.00	-40.3
CRB FOODSTUFFS (3/17) 1967=100	229.73	224.83	-5.6
CRB RAW INDUSTRIALS (3/17) 1967=100	305.07	302.51	-10.3

Sources: London Wednesday final setting, Chicago market, *Metals Week*, Memphis market, NYMEX, Commodity Research Bureau

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (3/18)	130.22	129.14	122.72
GERMAN MARK (3/18)	1.83	1.83	1.68
BRITISH POUND (3/18)	1.67	1.65	1.60
FRENCH FRANC (3/18)	6.12	6.14	5.67
ITALIAN LIRA (3/18)	1799.8	1803.5	1687.8
CANADIAN DOLLAR (3/18)	1.42	1.41	1.38
MEXICAN PESO (3/18)*	8.575	8.660	7.925
TRADE-WEIGHTED DOLLAR INDEX (3/18)	110.2	109.9	104.8

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars. Trade-weighted dollar via J.P. Morgan

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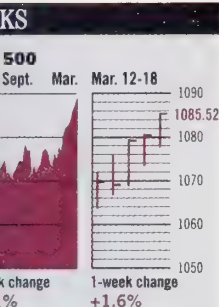
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Investment Figures of the Week



SENTARY
ing week for both the
ock market and the dol-
e Dow Jones industrial
e climbed four days
at, closing at a record
on Mar. 18. Brokerage
led the gain, spurred
eculation that Merrill
& Co. may be acquired
se Manhattan Corp. Oil
ny shares were propelled
ing crude prices. Mean-
the dollar rose to a two-
high against the yen.
ond prices fell on Mar.
nt of concern that the
ny has shown no signs
ing down.

U.S. MARKETS	Latest	% change	
		Week	Year
Dow Jones Industrial	8775.4	1.1	27.6
NASDAQ Combined Composite	1788.3	1.8	43.1
S&P MidCap 400	365.0	1.3	41.0
S&P SmallCap 600	197.2	0.8	39.8
S&P SuperComposite 1500	232.8	1.5	38.5

SECTORS	Latest	% change	
		Week	Year
Bloomberg Information Age	326.4	2.1	42.0
S&P Financials	134.1	3.5	47.7
S&P Utilities	242.2	2.0	25.6
PSE Technology	339.4	2.3	40.7

FOREIGN MARKETS	Latest	% change	
		Week	Year
London (FT-SE 100)	5903.6	1.3	36.3
Frankfurt (DAX)	4919.7	1.8	48.4
Tokyo (NIKKEI 225)	16,619.7	-0.8	-10.1
Hong Kong (Hang Seng)	11,121.7	0.0	-12.1
Toronto (TSE 300)	7426.8	1.1	22.0
Mexico City (IPC)	4844.4	2.2	25.3

FUNDAMENTALS	Latest	% change	
		Week ago	Year ago
S&P 500 Dividend Yield	1.43 %	1.44 %	1.86 %
S&P 500 P/E Ratio (Last 12 mos.)	27.1	26.5	20.8
S&P 500 P/E Ratio (Next 12 mos.)*	21.3	20.9	16.6
First Call Earnings Revision*	-3.51 %	-3.88 %	-1.08 %

TECHNICAL INDICATORS	Latest	Week ago	Reading
S&P 500 200-day average	951.2	945.6	Positive
Stocks above 200-day average	66.0 %	67.0 %	Neutral
Options: Put/call ratio	0.54	0.57	Negative
Insiders: Vickers Sell/buy ratio	2.01	1.69	Neutral

Data: Bloomberg Financial Markets; *First Call Corp.

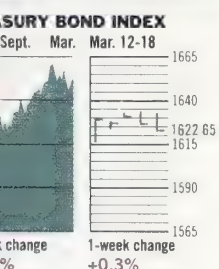
BEST-PERFORMING GROUPS	Last month %	Last 12 months %
Pollution Control	22.0	Homebuilding 93.6
Invest. Banking/Bkrgr.	18.6	Broadcasting 83.5
Homebuilding	17.1	Specialty Appar. Retailers 82.0
Engineering & Constr.	16.8	Invest. Banking/Bkrgr. 81.5
Steel	14.9	Communications Equip. 74.6

WORST-PERFORMING GROUPS	Last month %	Last 12 months %
Semiconductors	-9.9	Metals -36.7
Computer Systems	-4.5	Gold Mining -34.3
Photography/Imaging	-4.5	Shoes -30.3
Manufactured Housing	-3.9	Photography/Imaging -24.0
Oil-Well Equip. & Svcs.	-1.3	Hospital Management -14.0

BLOOMBERG MONEY FLOW ANALYSIS

Rebound ahead? Stocks with most significant buying on price weakness	Price	1-month change
IBM	100 ⁷ / ₈	-1 ¹ / ₈
Exxon	62 ¹⁵ / ₁₆	- ⁷ / ₈
Micron Technology	32	-3
Texas Instruments	55 ³ / ₈	-1 ¹ / ₈
Ascend Communications	33 ¹ / ₃₂	-1 ¹ / ₃₂
Sun Microsystems	43 ²⁹ / ₃₂	-1 ¹⁵ / ₃₂
Decline ahead? Stocks with most significant selling on price strength	Price	1-month change
Microsoft	80 ³ / ₈	3 ¹ / ₁₆
Dell Computer	62 ⁹ / ₁₆	5 ²⁹ / ₃₂
WorldCom	42 ⁵⁹ / ₆₄	4 ³ / ₆₄
Pfizer	89 ³ / ₈	3
PeopleSoft	49 ¹ / ₂	8 ¹ / ₁₆
Qwest Communications Intl.	39 ³ / ₈	5 ³ / ₁₆

REST RATES



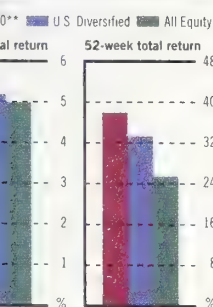
KEY RATES	Latest	Week ago	Year ago
MONEY MARKET FUNDS	5.12	5.13	4.96
90-DAY TREASURY BILLS	5.14	5.09	5.29
6-MONTH BANK CDS	5.07	5.08	5.04
1-YEAR TREASURY BILLS	5.33	5.37	5.79
10-YEAR TREASURY NOTES	5.57	5.63	6.74
30-YEAR TREASURY BONDS	5.91	5.93	6.99
LONG-TERM AA INDUSTRIALS	6.48	6.51	7.47
LONG-TERM BBB INDUSTRIALS	6.95	6.98	7.81
LONG-TERM AA TELEPHONES	6.78	6.82	7.67

BLOOMBERG MUNI YIELD EQUIVALENTS

Taxable equivalent yields on AAA-rated, tax-exempt municipal bonds, assuming a 31% federal tax rate.

	10-yr. bond		30-yr. bond	
	Latest week	Last week	Latest week	Last week
GENERAL OBLIGATIONS	4.42%	4.44%	5.02%	5.04%
PERCENT OF TREASURIES	79.36	78.86	85.02	84.89
TAXABLE EQUIVALENT	6.41	6.43	7.28	7.30
INSURED REVENUE BONDS	4.54	4.58	5.18	5.24
PERCENT OF TREASURIES	81.51	81.35	87.73	88.26
TAXABLE EQUIVALENT	6.58	6.64	7.51	7.59

UAL FUNDS



MANY ROADS LEAD TO THE TOP 50

Top-line growth is the holy grail in Corporate America, and times have never been better for achieving it. The cost of capital is low, global markets are opening everywhere (yes, Asia will come back), and real income is rising, thanks to higher wages and price disinflation. Opportunities to grow today are vast and varied. Yet myths about limits to corporate growth are deeply entrenched. They deserve a serious debunking.

Take the one about size. It used to be said that corporate behemoths could never grow as fast as startups. Maybe not. But as the *BUSINESS WEEK* 50 (page 76) shows, General Electric Co., weighing in at \$91 billion in sales, managed to boost sales by 15% and net income by 13% in 1997, a performance that's the envy of companies small and large.

And the myth about mature markets? Supposedly, it's impossible to generate as much growth in older industries as in hot, new ones. A cursory look at the *BW* 50 appears at first glance to confirm that assumption, since the top five companies on the list come from the fast-growing New Economy—computers, chips, and software. But then there are all those other high performers—PACCAR, Alcoa, Gap, NationsBank, and Chrysler. Trucks, aluminum, retailing, banks, and autos are all Old Economy industries, yet some-

how these companies can manage to wring out double-digit annual growth rates.

Our favorite myth is that there is only one right way to grow. Conventional wisdom says that growth by merger and acquisitions usually fails while internal, organic growth succeeds. So "bootstrapping," or buying companies using high-priced stock, boosts earnings per share for the new merged company. But, the argument goes, it's just dangerous math; the gain is illusory and doesn't last in the long run.

Not so in financial services. Sanford I. Weill's Travelers Group, No. 16 in the *BW* 50, uses acquisitions to improve distribution, go global, expand products, and increase efficiency of scale to save on costs. Buying Salomon Brothers is just the latest move in his strategy of buy to grow. Morgan Stanley used the same playbook in merging with Dean Witter.

Excuses wear thin for CEOs who can't go for growth. Behind all the strategies, one secret appears to be clear: gun for efficiency. Dell Computer Corp., for example, uses information technology to customize each computer, cutting out armies of middlemen while reducing the size of inventories. PACCAR does the same for long-haul rigs. Corporations still in the grip of myths about the limits to growth can't conceive of doing this kind of thing. They will forever lag behind.

TELECOM: LET THE FREE-FOR-ALL BEGIN

The Telecommunications Act of 1996 is not working. Designed to promote competition in cable and phone markets, it is instead being used to cement monopoly. It now is clear that campaign contributions to powerful legislators by competing interests produced deliberately obscure legal language. The result: paralysis in the courts. And attempts to balance different consumer and producer interests begat stifling compromises that worked only to block change. It's time for Senate Commerce Committee Chairman John McCain (R-Ariz.) to cut the Gordian knot. Partial deregulation is, in the end, an oxymoron.

What's needed is a true opening of all communication markets at once and a free-for-all fight among the competitors. That means ending laws and regulations that protect different constituencies in the communications business. Direct-broadcast satellite providers, for example, cannot offer local news and sports because of federal copyright laws. EchoStar Communications Corp. is meeting fierce resistance from cable and broadcast rivals, who contend that satellite-TV carriers can beam local programming only to households that can't get cable or broadcast television.

Weil, if cable can carry local programming—and under the "must carry" provision it is required to do so—why not DBS? Some 40 million people have gone into stores to ask about satellite TV, only to be told they can't get local stations.

Is it any wonder that only about 7 million, half in rural areas, have signed up? The strongest rival to cable and broadcast can't play on a level field because of copyright law.

The communications industry is defined by suffocating laws, regulations, and deals that block competition. During negotiations for the Telecom Act of 1996, the Bells made promises about entering local cable markets to provide competition and lower prices to consumers. In exchange, they wanted to be free to enter into lucrative long-distance phone services dominated by AT&T and MCI Communications Corp. Congress agreed, but only if the Bells opened up their own local phone monopolies. In the end, nothing happened. The Bells chose to fight in the courts to retain their turf. They ignored the cable market. And they lobbied regulators to elbow into long-distance without giving up anything. Net net, all monopolies were preserved, legislative intent notwithstanding.

Meanwhile, cable prices are rising at four times the rate of inflation, and consumers feel exploited. Cable companies say they must charge more for programming, yet many own the very same programs. They say customers are getting more channels, yet customers must pay whether they want them or not. It goes on and on. McCain should deliver a clean stroke that frees up all communications markets. Market forces may not always operate with complete efficiency, but Washington could create the monstrous snarl we now have.

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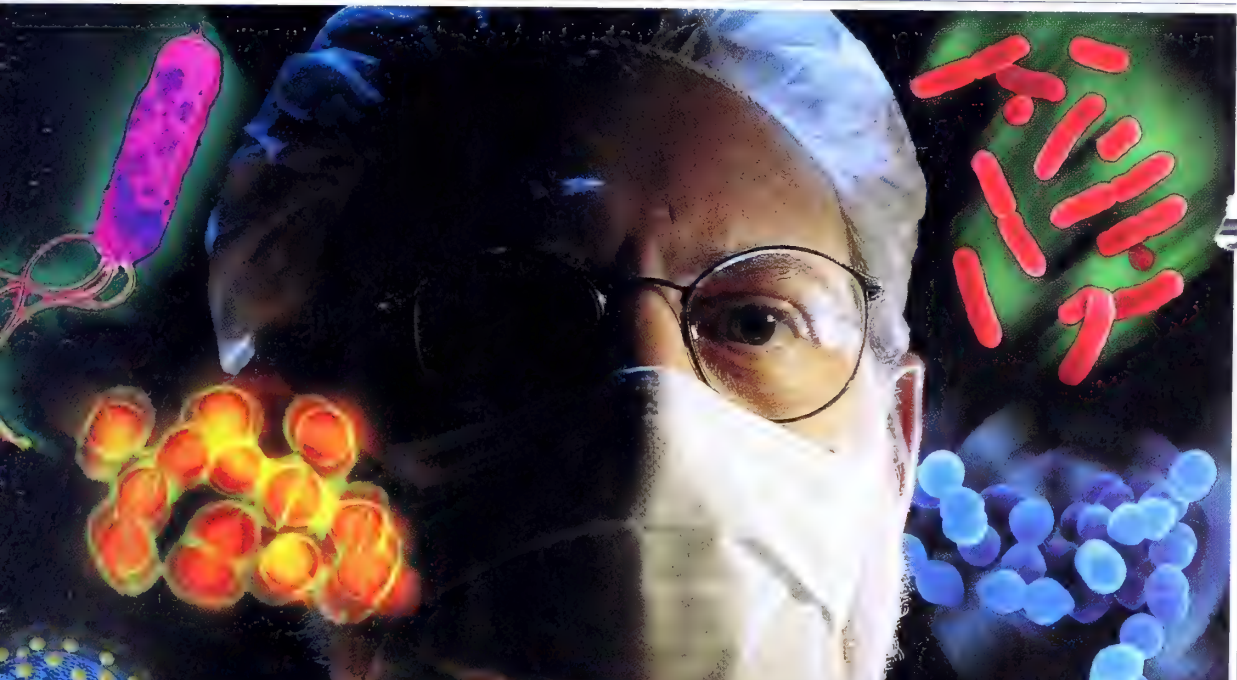
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BusinessWeek

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WAR *against the* MICROBES

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COVER STORY

WAR ON MICROBES

From hantaviruses to staph to tuberculosis, superbugs are making a deadly comeback *page 37*



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As deaths from infections surge, medicine is racing to regain control over antibiotic-resistant superbugs. Warriors in labs across the country search for ways to cripple deadly viruses and unlock the mysteries of lethal bacteria. And the revolution in molecular biology holds great promise. But the war may be lost unless campaigns are launched against the scourges that ravage poor nations, too

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use bill could sort out who would
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Up Front

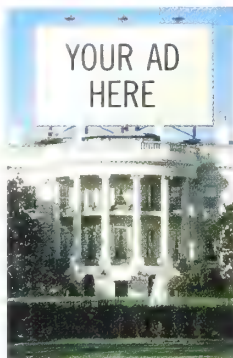
EDITED BY ROBERT McNATT

MEDIA MANIA

AND NOW, FROM THE WHITE HOUSE, AN AD

IT'S A POLICY WONK'S DREAM: a new public-affairs television station that airs entire press conferences from the White House or Pentagon. But wait a second—or 30. Unlike commercial-free C-SPAN, this station will sell ads to trade and public-interest groups. Will viewers appreciate, say, a Presidential press conference on the proposed tobacco settlement—sponsored by the Tobacco Institute?

Dennis Dunbar is betting they will. He is CEO and founder of Washington-based Information Super Station, Channel 28. Dunbar began ISS with \$2 million from a



videoconferencing business he owned. Started in February, ISS specializes in executive branch public-affairs programming and plans to go national this summer. Dunbar is sympathetic to the needs of lobbyists. Says he, with a straight face: "There aren't enough venues for people to reach out to try to promote their message."

So far, early sponsors may include a polling outfit, Club Tech. Still, the startup wins plaudits from C-SPAN, financed by the cable industry. Rich Fahle, C-SPAN's director of media relations, says: "It's a tough business, and an ad-based model is probably the only way to launch a C-SPAN-like service now." So, gun, beer, and tobacco lobbyists, line up. *Catherine Yang*

PAPER PLAYS

THE BIG BANG IS IN BONDS

THE NUMBERS WOULD MAKE any self-respecting Master of the Universe happy. The volume of corporate securities issued in the first quarter of 1998 has set a record, says Securities Data Co., which follows such things. Mostly, the surge is in bonds and other corporate debt.

Through Mar. 24, U.S. debt and equity issues totaled

\$437.4 billion, already surpassing the previous record of \$372.5 billion in the third quarter of 1997. Slightly more than two-thirds of that was straight bonds, and about one-fifth was mortgage- and asset-backed debt.

Why the love affair with the bond? Well, the yield curve has been flat: That's economist talk for low interest rates for longer maturities. Low rates drew foreign borrowers in droves, says SDC. Big offerings included the likes of the \$1.8 billion in notes sold by Cable & Wireless, a British telecom company.

Demand brings supply: Wall Street's bankers are successfully marketing their services and pushing debt instruments. For bankers, Q1 1998 was a very good quarter. □

HUGE NUMBERS

Issues of U.S. corporate securities this quarter are at record levels

	BILLIONS
STRAIGHT DEBT	\$297.7
MORTGAGE-/ASSET-BACKED DEBT	98.7
COMMON STOCK	24.1
ALL OTHERS	16.9

SOURCE: SECURITIES DATA CO.

TALK SHOW "Sex is not the one string on the guitar. There are nine more commandments."

—The Reverend Jesse Jackson, commenting on the Presidential sex scandals

SHOW BIZ

THE ROAR OF THE PLASTIC



FOOTLIGHTS: Broadway's Ragtime

THEY SAY FOR EVERY LIGHT on Broadway there's a broken heart. Producers are less sentimental; they'd be happy seeing a credit card for each of those bulbs.

They may. The League of American Theatres & Producers, Broadway's trade association, is preparing an official credit card. The Live Broadway affinity card, similar to programs offered by sports teams, should premiere around the time of the Tony awards in June. It's part of the

league's ongoing efforts to step up marketing for the \$1 billion industry.

The market is large. There are some 125 league theaters nationwide, of them in New York. Thirty million people saw a Broadway show last year.

more than total attendance in any pro sports league except baseball, says Michael Meurer, director of new-business development for the Broadway group.

What do you get with the card? No annual fee and "competitive" interest rates, says issuer First USA. Bonuses may include special seating at shows, backstage tour, good buys on theater memorabilia—even a walk-on part in a Broadway show. So what? This card could make you a star.



UP IN THE AIR

COFFEE, TEA, OR ANOTHER AIRLINE?

IMAGINE IF BURGER KING rewarded frequent diners with a meal at McDonald's. Well, AirTran Airlines, formerly ValuJet, has unveiled just such a frequent-flyer program—free trips on other airlines. Its ads boast that its frequent-flyer program is "the fastest way to earn a free ticket on Delta." Why promise passengers the chance to fly with a rival?

With the major carriers of ten-matching its low fares, "the tie-breaker becomes frequent-flyer programs, and we

lose," explains M. Ponder Harrison, senior vice-president for marketing. Customers who book 12 coach or six business-class roundtrips by Dec. 31 can get a ticket on another carrier. That's double the flying needed for an award on AirTran.

AirTran, which serves 15 eastern cities, will buy tickets on several airlines, but won't book a ticket to a destination it serves. It presumes many award-winners are heading west. Miami aviation consultant Robert Booth says the program is "a smart marketing move, but I question the economics." Harrison replies: "AirTran will find the cheapest tickets. As a low-cost carrier, that's something it knows about." *Gail DeGeorge*



Product: Nose Glasses

Distribution:
Toy Merchants, Specialty Shops

Sales Plan:
Increase sales by 20% in Q3

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CAR TALK

SO THIS MOOSE SAYS TO THE MECHANIC...

HEARD THE ONE ABOUT THE new Mercedes-Benz perfume? It smells like a moose and makes people fall over. If you don't get the joke, you haven't been following the travails of the new Mercedes A-class car, introduced in Europe last fall. Mercedes is trying to overcome a public-

relations fiasco after its car flipped over during a "moose avoidance" test set up by a Swedish auto magazine. The incident prompted plenty of jokes that Mercedes says it may actually publish as *The 100 Best Moose Jokes*.

Customer to a Mercedes dealer: "How quickly can you deliver the new A-class?" Dealer: "You're in luck! There's still one lying around outside."

What do you call 100 A-classes lined up in a row? Dominoes.

Right after the accident, Mercedes worked to improve the car's stability. Polls showed that the company gained sympathy for admitting that its renowned engineers had blown it, and sales began to rebound. Mercedes now says it has a new revenue stream from the A-Class: renting out the underside of the cars as billboards. Hey, just kidding, just kidding. *David Woodruff*

OVER THERE

THE WIRELESS FUTURE IS—FINLAND?

IF THERE WERE AN OLYMPIC event for mobile-phone use, Finns would likely win the gold, silver, and bronze. Four of every 10 Finns have a mobile phone, and surveys say 90% will by 2000. So it's not surprising that Finns are pretty darn good at finding new uses for the things.

Want your car washed? Telecom Finland and Esso have launched a new "Mobile Car Wash" service at a gas station near Helsinki. Customers use the mobile phone to dial a special number, akin to a 900 number in the U.S., that approves the payment before it is added to the phone bill. The Finnish "dial-a-wash" is a hit with the sta-



tion manager, who says it speeds up service.

But Telecom Finland's plans for getting folks to use phones instead of cash or credit cards don't end at the car wash. The company has launched an experiment with a Coke vending machine at the University of Technology in Helsinki. And at two Helsinki restaurants, you can even dial up tunes on the jukebox with your phone. "We see the mobile phone providing all sorts of everyday services," says Telecom Finland Vice-President Jari Jaakkola. "These are just the first quick and dirty applications." More are on the way. *William Echikson*

DRAWN & QUARTERED



PERK PLEASURES

MARY KAY'S OFF-ROAD BONUS

EVERYBODY IN THE BEAUTY business knows that selling enough lipstick or eyeliner gets you the use of a pink Cadillac DeVille at Mary Kay. It's the top prize for the most productive salespeople at the cosmetics company.

But tastes in cars change. So does Mary Kay's automobile incentive program. Now the company has added a sport-utility vehicle, a white GMC Jimmy, to the lineup. It doesn't replace the Cadillac, but, says spokeswoman Karen Dodge, "we like the idea of being able to offer women choices."

In Mary Kay's pecking order, the Cadillac goes to the top producers, a pink Pontiac

Grand Prix to the next best, and a red Grand Am to the third tier. The Jimmy, available since January, is now an alternative to the Grand Prix. To get it, sales director's units must total \$75,000 in sales in six months and maintain a monthly pace of \$12,500 in sales for the next



JIMMY: Not so pretty in pink?

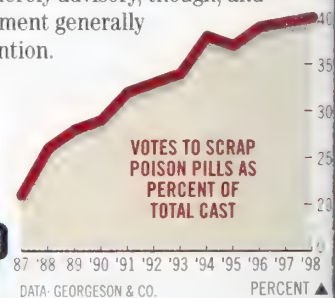
two years. Winners can use any car for only two years.

Mary Kay, with 10,000 cars, claims the largest commercial fleet of GM passenger cars in the world. Still, what's good for GM in the U.S. falls flat internationally. Top sellers in Russia get a Volvo.

THE BIG PICTURE

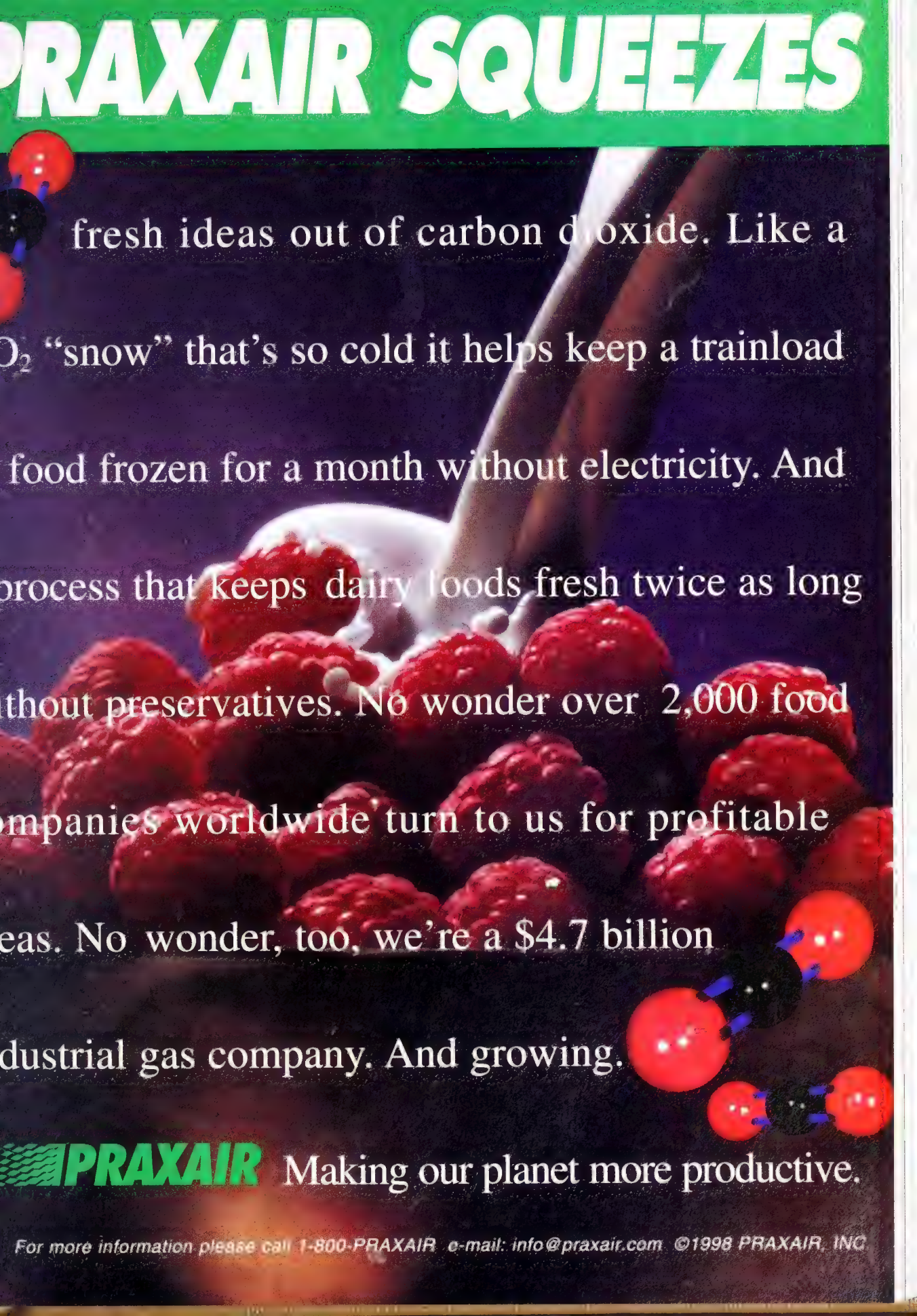
POISON PILL ANTIDOTE

More shareholders are voting against poison pills—defenses that make takeovers more difficult. Most such resolutions are merely advisory, though, and so far management generally pays no attention.



FOOTNOTES Frequent fliers who try to fly an airline with the best food: **56%**. Those who would pay more for top cuisine: **26%**

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AN HONOR FOR NEW MEDIA

As cyberspace gets more crowded, most Web sites have to struggle for recognition. But Business Week Online has just been singled out by the judges of the National Magazine Awards as a finalist in New Media for the second year in a row. We're extremely proud of this honor, coming as it does from our peers in the magazine industry, where competition online is as intense as in print.

Over the past year, Business Week Online has steadily increased in size and sophistication, and our audience has grown significantly. We've added regular investment and personal finance features in

our Daily Briefing area, an Interactive Mutual Fund Scoreboard in Investors Central, and many more online-only supplements to each week's magazine (see our online versions of the BW 50 and Standard & Poor's 500 from the Mar. 30 issue).

Our goal is to keep improving Business Week Online—and keep working hard to stay in the front of the growing cyberpack. Please visit us soon at www.businessweek.com or on America Online at keyword: BW.

Stephen B. Shepard
Editor-in-Chief



AETNA SETS THE RECORD STRAIGHT

I am astounded that BUSINESS WEEK could so wrongly interpret Aetna's strategy ("Aetna's Brave Old World," Finance, Mar. 30). This strategy has been clearly and consistently articulated the same way for the past three years.

I am equally mystified as to how anyone could miss the point that the \$1 billion acquisition of NYLCare, a managed-care company with 2.2 million members, represents "another important step in our strategy of continuing to grow our health business," as we stated in our Mar. 16 press release announcing the deal. To conclude otherwise defies all logic.

Abandoning our strategy would make no sense at a time when managed care, which meets the customer need for access to affordable, high-quality

health care, continues to grow double-digit rates. We were a leader in managed care prior to this acquisition, which unquestionably strengthened our position.

In addition, among the other numerous inaccuracies in your story is a serious misstatement of fact that is misleading to our customers: Far from having been sold, our annuity business is going strong, with more than \$1 billion in customer assets under management at yearend 1997, up 23% over 1996.

Further, I never made the statement that "we are an insurance company." What I have said consistently since 1995, when we decided we could no longer be all things to all people, Aetna's strategy has been to focus on the two areas that matter most to people—their health and the financial security—and to be a leader in those businesses in the U.S. and

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lected international markets.

Richard L. Huber
President and CEO

Aetna
Hartford

's note: The story misstated Aetna's strategy. We regret the error.

ON DICKINSON: SAFE LES ARE EASY TO FIND

Our article "Locked out of the hospital" (Social Issues, Mar. 16) on health-care group purchasing organizations contains several implications re- to health-care worker safety, in- tion, product quality, and trade ces. It suggests that there is only company providing products that t health-care workers against ac- al infection, and that this small, "ative" company is being locked f the market, thereby denying als the opportunity to protect pa- and caregivers.

In reality, Becton Dickinson & Co. umerous other companies develop apply safety products to the mar- n the case of Becton Dickinson, f total U.S. revenue in fiscal 1997 he three businesses offering ps" and related products came the sale of safety products and es. Becton Dickinson, one of the t companies in the medical tech- y industry, pioneered the devel- of safety products over 10 ago.

The story describes an isolated prob- at was experienced by Becton nson last year with a prepared l-media product, and it suggests atients were potentially at risk. as never the case. When this ssue arose, our employees d around the clock to ensure that als received high-quality product ed from a second Becton Dickin- ant.

ally, the article refers to allega- that GPO contract negotiations ly restrict free trade. As in all usiness dealings, Becton Dickin- negotiations with Premier Inc. ntirely legal and ethical in every ct.

Clateo Castellini
President and CEO
Becton Dickinson & Co.
Franklin Lakes, N.J.

PERILS OF MAKING BEAUTY 3 QUALIFICATION

Robert J. Barro's "So you want to the beautiful. Well, why not?" omic Viewpoint, Mar. 16), the only Barro proves is that we are a so- that values physical beauty over

merit. What standard of beauty is Mr. Barro referring to?

As a white male (kudos to BUSINESS WEEK for providing a photo), he obviously has never experienced the discrimination women face every day as we are judged by our bodies, faces, and dress. How does he think it feels knowing that one has been hired first because of appearance, secondarily [because of] ability? Are these the hiring standards used at Harvard University?

If we are to follow Barro's reasoning, it is my right as a consumer and taxpayer to dictate the physical qualities necessary for my patronage of a business or service. As a young, heterosexual woman, I am tired of seeing unattractive, middle-aged white men everywhere. In fact, I would appreciate seeing more young, beautiful doctors, chief executive officers, and academics. As Mr. Barro asserts, this quality is just as valid as intelligence, ability, and merit. If I get my way, Mr. Barro, I'm

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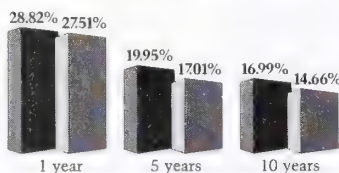
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Readers Report

CORRECTIONS & CLARIFICATIONS

"Palmy days for 3Com?" (Information Technology, Mar. 16) should have stated that the AstroPilot is an astronomy reference tool.

sorry; Tom Cruise will have to replace you at Harvard.

Lisa Nielson-Hathaway
Albany, N. Y.

'THE TOUGHEST STANDARDS IN THE NATION': CalPERS

We expect critics to call us on the carpet when we're not responsive to issues, but when we act swiftly to create sweeping ethics standards, the fact should be reported fully ("Governance doc, heal thyself," News: Analysis & Commentary, Mar. 16). Our board's standards are the toughest in the nation—ban on political contributions, a policy of contractor disclosure of financial ties, enhanced openness about investment decision-making, monthly gift-reporting requirements, and a no-contact rule for contractors from the date that a competitive bid document is mailed.

James E. Burton, CE
California Public Employee
Retirement System
Sacramento

COUNTING THE FRENCH IN SILICON VALLEY

"Go West, young Frenchman" (International Business, Mar. 9) contains certain number of inaccuracies. The number of French citizens registered at the Consulate General of France in San Francisco is not 40,000 but 13,900. The number of the registrations has not quadrupled since 1991. At that date, it was 10,400. By definition, it is impossible to know the number of nonregistered French citizens. But there is no reason that number should increase more than the number of registered citizens.

André Parar
Consul General of France
San Francisco

Editor's note: Several sources, including government officials, confirmed the 40,000 French expatriates are estimated to be living in and around Silicon Valley.

DID GEICO GET A BAD RAP?

Howard Gleckman's "Steering you to a car insurer to a fair deal" (Personality)



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Readers Report

ss, Mar. 9) could have shown
ers how the insurance process
after a car is stolen, but his re-
as incorrect. Geico's original offer
41 more than he said. The dif-
e between Geico's initial offer
amount accepted by Gleckman
78, not \$1,156. The 16-page con-
s' report used to help determine
value listed 16 other '90 Ac-
not just three. (We offered him
the highest nor the lowest val-
ong all these cars.) Questioning
jectivity of the report because
y for it is ridiculous. The report
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George W. Rogers
Vice-President
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's note: Gleckman disagrees with
numbers.

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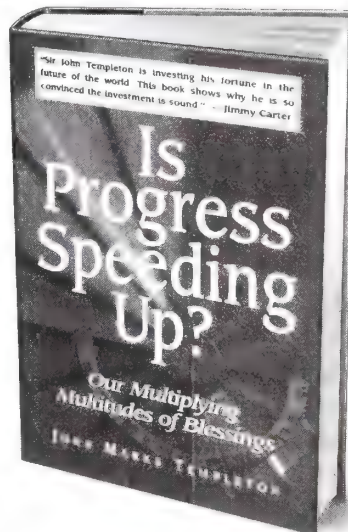
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Sir John Templeton's new book is bad news for pessimists.

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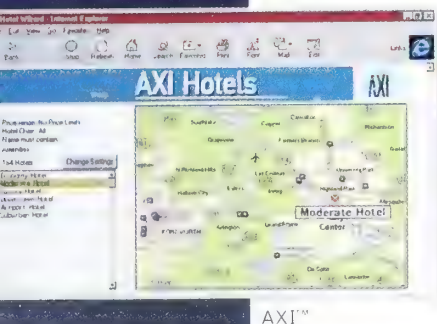
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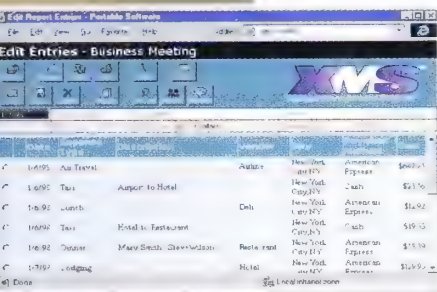
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THE GREAT BETRAYAL:

How American Sovereignty and Social Justice Are Being Sacrificed to the Gods of the Global Economy

By Patrick J. Buchanan

Little, Brown • 320pp • \$22.95

TILTING AT THE FREE-TRADE DRAGON

I was having lunch with author and Canadian political activist Maude Barlow, listening to her explain why Canadians must be protected from foreign news media by content quotas and investment controls on magazines, television, and books. "Canadian journalists are best able to interpret the news for Canadians," she insisted, adding: "Of course, I'm no Pat Buchanan, either."

But guess what—Patrick J. Buchanan agrees with her views. "If Canada wishes to retain her cultural identity and restrict the flood of U.S. magazines, TV shows, and films, why are Canadians wrong?" asks the TV pundit and two-time contender for the GOP Presidential nomination in *The Great Betrayal: How American Sovereignty and Social Justice Are Being Sacrificed to the Gods of the Global Economy*.

In fact, Barlow and much of the U.S. public may be closer to embracing Buchanan-omics than most of them realize. As international trade has grown during the 1980s and '90s to dominate much of the U.S. economy, it has done a lot of good. But so too has it brought out the bad—wage stagnation, drug trafficking, environmental degradation, sweatshop and child labor. And it has been the negative effects that have been in the news. Now, Buchanan, largely ignoring the good that trade also accomplishes, makes the case for recognizing another of trade's deleterious effects: the loss of national political control that comes with globalization and free trade pacts. Here Buchanan resides amid an odd but ever-growing league of nationalists across the political spectrum that includes Barlow, Ralph Nader, General Suharto, and Mexican corn growers.

Buchanan's best argument is this: Economic policy—"enlightened nationalism"—ought to benefit a nation and its people, not some one-world ideal

found nowhere outside economic textbooks. "The economy is not the country; the country comes first," he says. But that's changing rapidly, he notes. In Washington, instead of patriots, Buchanan finds international trade policymakers who serve the interests of rootless "transnationals" such as Boeing, ConAgra, and Motorola. These giants are heartlessly abandoning America for "a Darwinian world of the borderless economy, where sentiment is folly and the fittest alone survive. In the eyes of this... elite, men and women are not family, friends, neighbors, fellow citizens, but 'consumers' and 'factors of production,'" he laments.

Standing in contrast, Buchanan says, are such Americans as Roger Milliken, founder of textile company Milliken & Co., and Aaron Feuerstein, CEO of Malden Industries Inc. When textile plants of each company burned down in Georgia and Massachusetts, respectively, workers were kept on the payroll and plants rebuilt. That made them "conservatives of the heart."

Buchanan hasn't always been so tenderhearted, of course. As a speechwriter in the Reagan White House, he once happily prepared a veto message for a textile-protection bill sought by Milliken. Moreover, when he has exhibited passion in the past, it has been to defend accused Nazi war criminals, criticize immigration, and attack liberals, homosexuals, feminists, Democrats, and Israel. As a result, he has been widely accused of anti-Semitism, xenophobia, and homophobia.

The Great Betrayal provides Buchanan another opportunity to flail

wildly at the reactionary gong with such statements as this: Globalization is causing allegiances to shift "from nation to ethnocentrism," leading to segregated student dorms, ethnic anger, and Shiite militias, while impelling a breakup of Canada, Britain, and Italy.

Unfortunately, these sorts of diatribes often overshadow Buchanan's legitimate and worrisome message that U.S. citizens are losing control of the economy. He also errs by giving too much credence to the supposed benefits of high tariffs in U.S. history. As proud protectionist, Buchanan places himself among Presidents Washington, Lincoln, McKinley, and Teddy Roosevelt. "Protectionism, then, is not some alien dogma," writes Buchanan. "It is America's own invention, the defense perimeter of the world's greatest free-trade zone, an integral element of the American free-market system, and an indispensable contribution to national prosperity." Certainly, tariffs helped nurture

fledgling U.S. manufacturing. But even Adam Smith recognized the "infant industry" justification for tariffs.

So, naturally, Buchanan proposes higher tariffs—phased-in 15% tariff on imports and a corresponding cut in income taxes. Other tariffs would be adjusted country-by-country basis to equalize wage rates and currency fluctuations. Japan and China would be hit with special tariffs in retaliation

for their unfair-trade practices. But Buchanan fails to address the result: the world economy if others follow suit. Nor does he recognize the consumer to be as important as the producer of goods, or that higher standards of living due to lower consumer prices are also an outcome of trade. Besides, what if Canadians prefer watching *Minutes* or Jerry Springer to the so-nambulant Canadian Broadcasting Corp.? Shouldn't they be allowed?

Buchanan may find himself carrying *The Great Betrayal* as his campaign manifesto in 2000. If so, he'd better prepare to answer a lot of questions about trade economics.

BY PAUL MAGNUSSON

Magnusson covers trade and global economic policy from Washington.

PATRICK J. BUCHANAN



HOW AMERICAN SOVEREIGNTY AND SOCIAL JUSTICE ARE BEING SACRIFICED TO THE GODS OF THE GLOBAL ECONOMY
THE GREAT BETRAYAL

BUCHANAN TRUMPETS THE MESSAGE THAT U.S. CITIZENS ARE LOSING CONTROL OF THE ECONOMY

How one telecom exec is using Clarify to make new friends and keep the old.

Bob Rouse, Executive VP Engineering Systems & Operations



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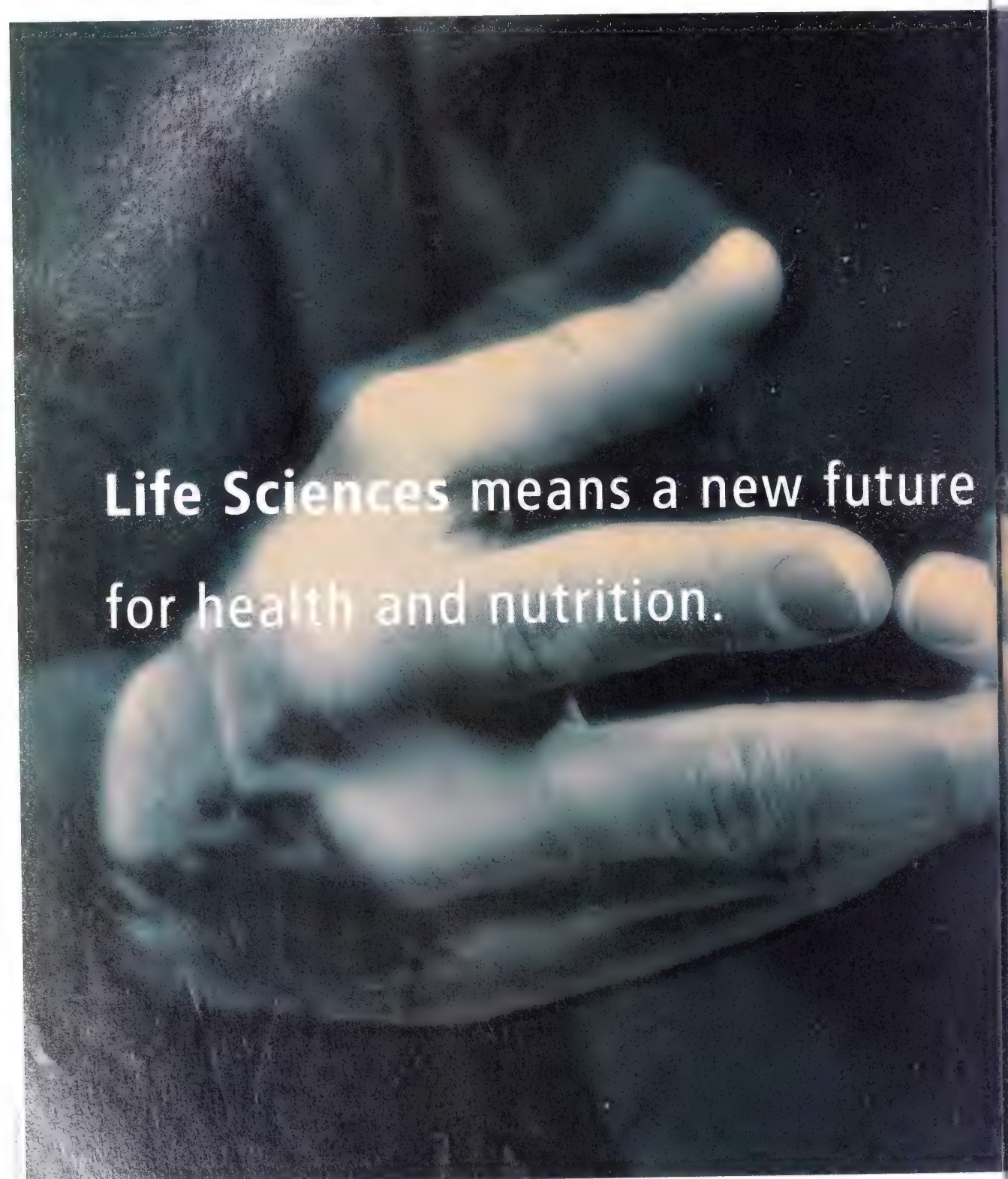


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THE BUSINESS WEEK BEST-SELLER LIST

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- 1 THE MILLIONAIRE NEXT DOOR** by Thomas J. Stanley, PhD, and William D. Danko, PhD (Longstreet Press • \$22) *The penny-pinchers shall inherit the earth.*
- 2 DIE BROKE** by Stephen M. Pollan and Mark Levine (Harper-Business • \$25) *Forget about the will—and the conventional wisdom, says a financial adviser.*
- 3 YOU HAVE MORE THAN YOU THINK** by David and Tom Gardner (Simon & Schuster • \$25) *Help for the investment-challenged.*
- 4 CHARLES SCHWAB'S GUIDE TO FINANCIAL INDEPENDENCE** by Charles R. Schwab (Crown • \$23) *Tips from the discount brokerage CEO.*
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Reviews and more are available on AOL (Keyword: BW) or www.businessweek.com (Click on BW Plus!)

HOT TYPE

THE TITLE IS SCARY—AND THAT'S JUST THE beginning. In *Die Broke*, the No.2 hardback on this month's best-seller list, financial consultants Stephen M. Pollan and Mark Levine offer depressing money-management lessons. Your career may be soaring today, but a soft landing probably doesn't await you at the end, augur the authors. Get ready, boomers: In this life, you're on your own.

Their formula for survival? "Quit today, pay cash, don't retire, die broke." The first of these is deceptive: No, you don't really get to quit. Rather, the authors mean you should "abandon any remaining tinges of loyalty to your employer" and always be looking for another, higher-paying job. Then, toss your credit cards and live frugally. Forget retirement, "an idea that worked for one

generation only" as a result of demographics favoring today's seniors. Finally, plan to use up all of the nest egg you constructed leaving nothing to heirs.

Die Broke provides a useful glossary on such subjects as charitable remainder trusts and reverse mortgages. But first, readers have to endure a fright fest. On pensions we're told: "Most of you will be fired long before you're vested." On consumption "make spending as difficult and uncomfortable as possible." On life after 50, we're advised to emulate the Japanese, "while continue on the job...as 'temporary workers'...giving up seniority and promotions and accepting equivalent cuts in their income." Hey, Stephen King fans, it doesn't get any better than this.

BY HARDY GREEN

STEPHEN H. WILDSTROM

HANDHELDS STILL HAVE A WAY TO GO

latest models' screens look great, but their weak software is limiting

What a difference color makes. When I first looked at handheld computers built to use Microsoft's Windows CE software about 18 months ago, I thought the attempt to imitate the look and feel of desktop Windows—designed for big color screens—on a tiny gray display didn't work very well. Now, color handhelds are on the market. The devices still seem too large to fit into a pocket, but they are more user-friendly and more useful for true on-the-go typing. But they can be useful to folks who use E-mail, light-word processing, and custom programs.

CONVENIENCE LOSS. Color handhelds imposes some trade-offs. The new models from Hewlett-Packard, Sharp, and Hitachi, and upcoming products from NEC and LG Electronics, cost about \$1,000. That's \$400 more than monochrome models. Perhaps more significant, the monochrome displays get 20 hours or so of use from a pair of AA batteries, while color models get only six to eight hours from a single chargeable. That should be plenty of power to get through a day's work, and you can always carry a spare. But you lose the safety net of a backup agency fallback of simply switching in a couple of avail-

able-anywhere alkaline cells.

After spending some time with both the \$859 HP 620LX and the \$999 Sharp HC-4500, I think the advantages of color are well worth the cost. Not only are the windows much easier to recognize in color but in poor light especially, the bright, backlit screens are much easier to read than the original gray.

These similar models use calculator-style keyboards that are unsuited for serious typing, though I found the



HP 620LX: *Easier on fingers but harder on batteries*

HP model's bigger keys easier to use. The Sharp justifies its higher price with a built-in 33.6 kbps modem that's much easier on the batteries than the PC Card modem required by the HP.

Microsoft has improved Windows CE in version 2.0, but much remains to be done. For example, the original Windows CE E-mail program was so bad as to be almost unusable. You could not, for example, receive any file attachments.

The new program is much

better but still flawed. It does let you download file attachments, but it doesn't use the latest technology that allows remote users to manage mail on servers efficiently. Nor does it give you access to public or corporate E-mail directory servers.

Similar limitations hobble other applications, which must be kept small because the handheld PCs lack disk storage. Pocket Word, for example, cannot display or create justified text. Pocket Excel supports only a small subset of the desktop worksheet's built-in functions, omitting, for example, most statistical calculations.

ECLIPSED ALREADY? These software limitations are frustrating to anyone who would like to use a handheld PC as a laptop substitute. This is especially unfortunate because some handhelds that are coming out soon could fill the bill. Both the NEC MobilePro 750C and the LG Electronics Phenom Ultra will offer displays measuring about eight inches diagonally (vs. 6.5 inches in the HP and Sharp versions) and nearly laptop-size keyboards.

Later this year, Microsoft will release a third version of Windows CE, code-named Jupiter, that will move handhelds closer to laptops. Jupiter will support 640-by-480-pixel displays, compared with the current 640-by-240 screens. The additional pixels provide a much more laptop-like display that shows twice as much information, making it far more suitable for spreadsheets and word processing.

Weighing in at two to three pounds, Jupiter machines could be very attractive alternatives to six-pound laptops for many uses. The question is whether Microsoft will come up with the software needed to do the job.

BULLETIN BOARD



HARDWARE

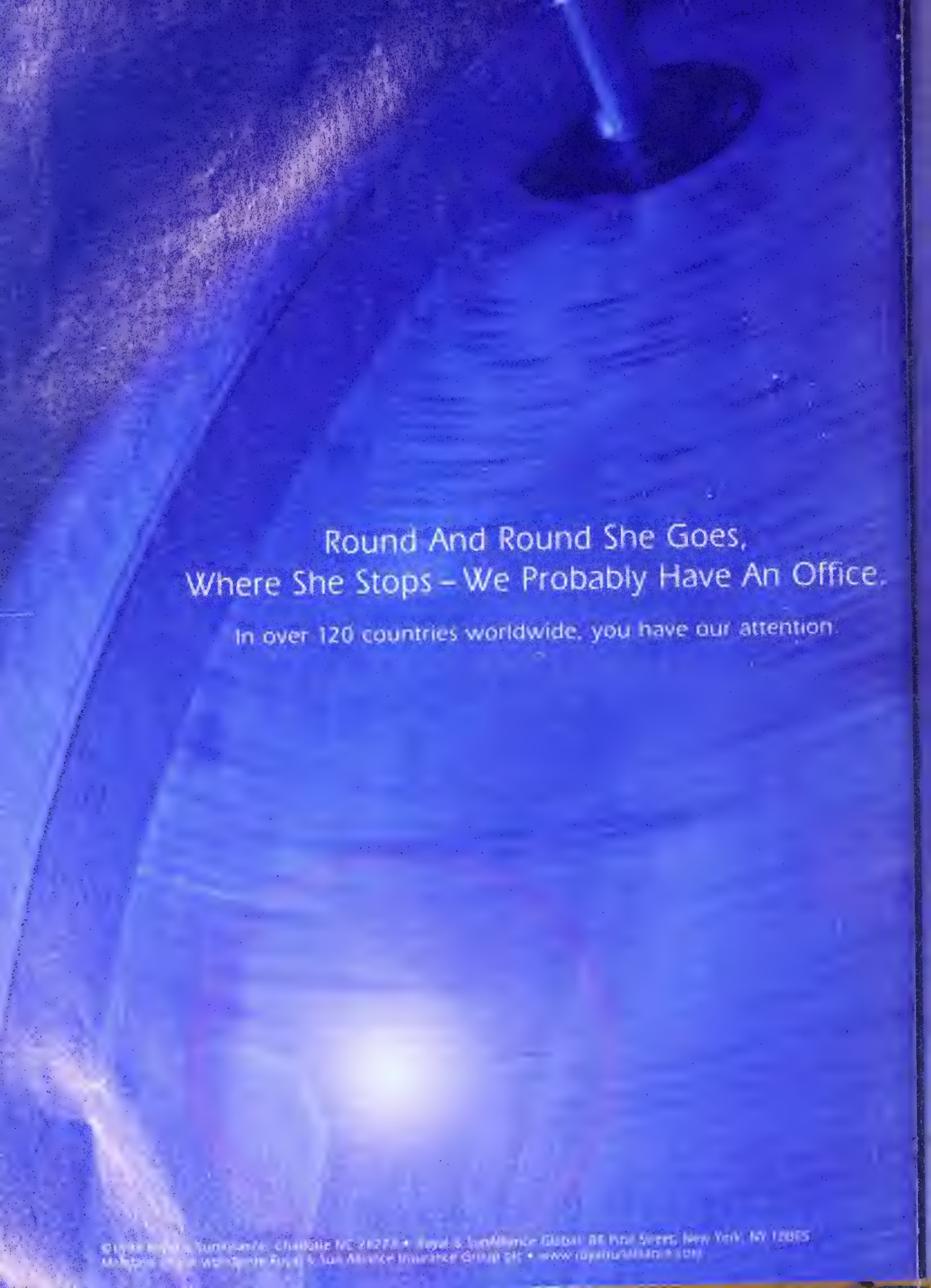
THE PROFESSIONAL'S MAC

The long wait for high-performance versions of Apple Computer's G3 Macintosh is over. Apple is shipping 300-Mhz models designed for multimedia professionals, with prices starting at \$3,399. The top-of-the-line version, at \$4,899, features 128 megabytes of memory, two video adapters for use with dual monitors, and two high-performance, 4-gigabyte hard drives. But these models use the same minitower cases introduced for the original G3s—a potential problem for pros who want to add video-capture boards and other multimedia goodies. The high-end configuration ships with only one free expansion slot.

SUITE WARS

CONCESSIONS TO OFFICE 97

If you can't beat 'em, work with 'em. That's what Lotus Development and Corel are doing as they struggle against Microsoft's dominant Office 97 Suite. Corel is offering a free upgrade to its WordPerfect Suite 8 that makes it easier to read and write Microsoft Word files. Lotus' upcoming SmartSuite Millennium Edition adds an optional set of menus that makes the screens of Lotus WordPro 97 and 1-2-3 resemble those of Word and Excel. And a new feature, called FastSite, automates the publication of documents, including those prepared in Office, on a Web server.



Round And Round She Goes,
Where She Stops – We Probably Have An Office.

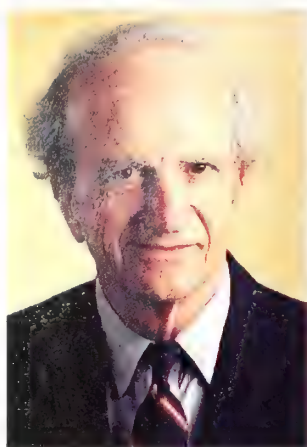
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BY GARY S. BECKER

LET THE MARKETPLACE JUDGE MICROSOFT



RELAX:
In rapidly
changing
high-tech
industries,
monopolies
tend to be
temporary.
Just look
at IBM

The government's antitrust suit against Microsoft Corp. raises important economic and public-policy issues about the dynamics of monopoly power in industries undergoing rapid technological change. Unfortunately, these issues have been obscured by the bashing of a company that is unpopular with both competitors and politicians.

Computer operating systems involve network externalities, whereby new users raise the benefits to others on the same system. Other networks, including telephone and stock exchanges, work in similar fashion. Members of the same system can communicate easily with each other, while members of different systems have greater trouble.

Competition among companies with different systems tends to eventually produce a single network standard that connects practically all users, the way Microsoft's Windows has managed to get about 90% of the market for operating systems. There is a growing call for government regulation of networks when inefficient systems become standard because aggressive companies gain an early adoption of their systems.

One frequently cited example of an alleged inefficient standard is the keyboard—the "qwerty" system named after its first six letters. However, economists Stan Leibowitz and Stephen E. Margolis have found no support for the claim that qwerty was inefficient when adopted. They also marshal persuasive evidence against allegations that the defunct Betamax videotape format was much better than the adopted VHS or that DOS and PCs prevailed over a superior Macintosh.

If highly inefficient systems did become standard, companies that had much superior products would use low prices and other attractions to take customers away from the less efficient systems. Government bureaucrats, lawyers, and judges cannot set better standards than the marketplace, especially in sectors with fast-changing technologies.

"CREATIVE DESTRUCTION." It's true that companies controlling efficient standards can have monopoly power, which can generate high prices for their products. However, in industries with very rapid technological change, such as the computer industry, monopoly positions tend to be temporary. The reason is that entrepreneurs find ways to develop better technologies so that they can leapfrog

dominant producers. Rapid turnover of monopolies in dynamic industries such as computing suggests that antitrust policy should focus not on whether companies have large market shares but on how soon they are likely to be replaced by others with superior technologies.

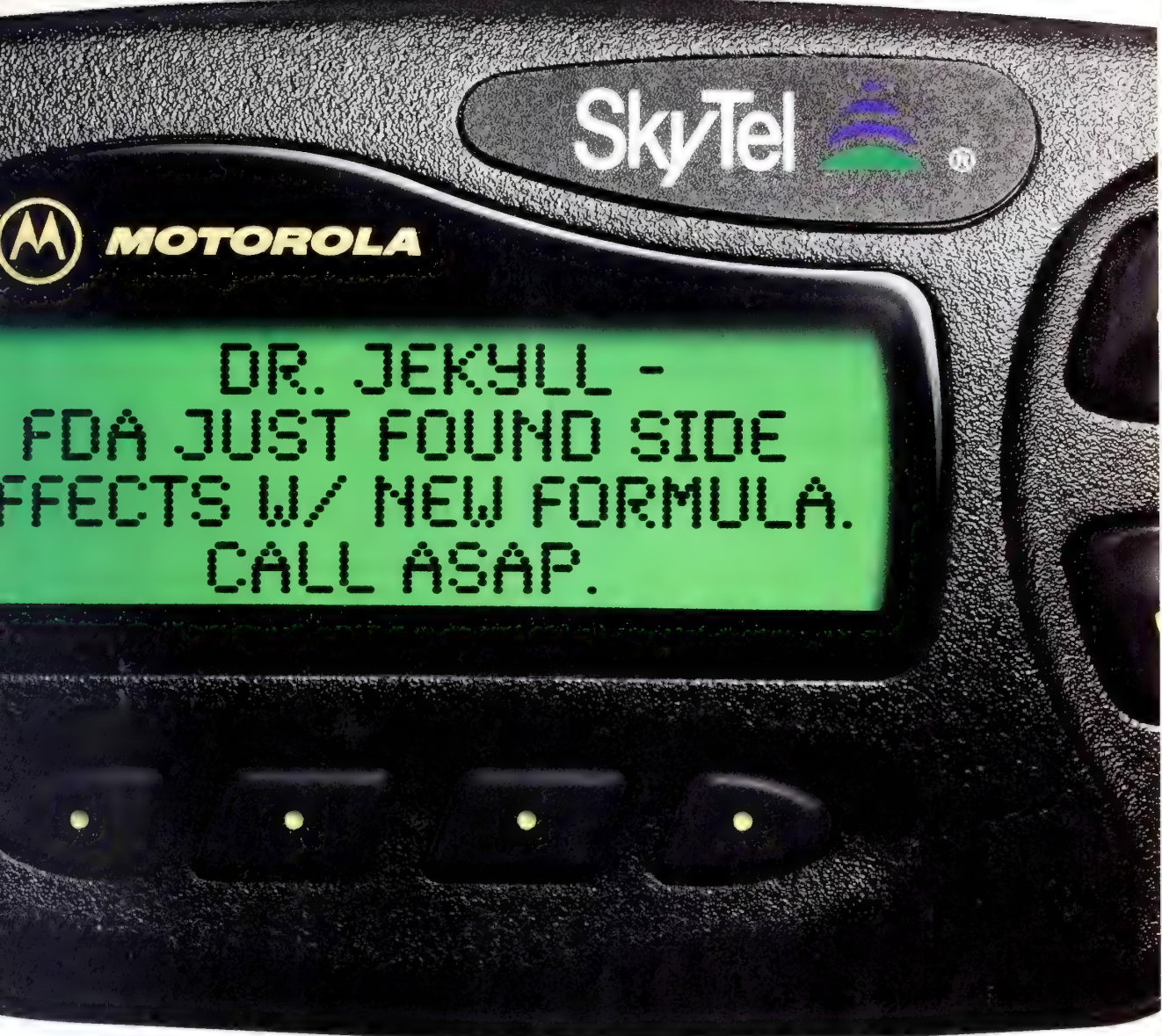
This "creative destruction" by entrepreneurial activity is not merely theory. IBM monopolized mainframe computers in the early days of the industry. But the company missed the turn on PCs, and its market value declined enormously while it was surpassed by upstarts. Wireless phones, fiber-optic wire, and special services for business helped Motorola, Ericsson, and others destroy the monopolies of government-regulated telephone companies such as AT&T.

PREDATORY PRICING? Companies that control operating systems are alleged to leverage their monopoly power in one market so as to gain dominant positions in related products. Microsoft's attempt to combine its own Internet browser with its Windows operating system is the immediate reason for the present Washington antitrust investigation of that company. However, leveraging monopoly power hardly describes what Microsoft is doing. A typical tie-in to extend economic power involves charging a monopoly price for the tied product, yet Microsoft gives the browser away.

Some politicians and competitors of Microsoft, such as Netscape and Sun Microsystems, respond that the company is engaged in so-called predatory pricing by giving its browser away. They argue that Microsoft will greatly raise prices in the future after its competitors are forced out. Companies that price aggressively have been accused of predatory pricing, but the legal suits over this issue have rarely concluded that the accused companies jacked up prices after competitors exited. Presumably, the reason is that other companies would enter and take business away if they tried to do that.

Several novel economic issues arise in industries with network economies. But we should resist proposals for greater government oversight of computing and other network industries with rapid progress. Competitors that develop superior technologies are far better protectors of consumers than government officials and bureaucrats who march to the beat of political popularity.

Gary S. Becker, the 1992 Nobel laureate, teaches at the University of Chicago and is a Fellow of the Hoover Institution.



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WHAT'S THE DIFFERENCE BETWEEN A LITTLE KID WITH A WEB SITE AND A MAJOR CORPORATION WITH ONE? NOTHING. THAT'S THE PROBLEM.

Building a publishing-only Web site is the first step to becoming an e-business. A step that most businesses (and a lot of little kids) have already taken. That's fine as far as it goes – it's a very cost-efficient way to distribute basic information.

But the real payoff (for businesses, at least) comes with steps two and three. Step two is moving to "self-service" Web sites – where customers can do things like check the status of an account or trace a package online.

Step three is moving to transaction-based Web sites – not just buying and selling, but all processes that require a dynamic and interactive flow of information.

IBM has already helped thousands of companies use the Web to make the leap from being a business with a Web site to being an e-business – putting their core processes online to improve service, cut costs or to actually sell things.

For example, we helped Charles Schwab Web-enable their brokerage systems for online trading and customer service. Since opening, Schwab's Web service has generated over one million online accounts totaling over \$68 billion in assets.

e-business economics are compelling. According to a recent Booz-Allen & Hamilton study, a traditional bank transaction costs \$1.07; the same transaction over the Web costs about 1¢. A traditional airline ticket costs \$8 to process; an e-ticket costs just \$1. Customers love the convenience; management loves the lower costs.

IBM solutions have already helped thousands of businesses become e-businesses. To find out how IBM can help you do the same, bookmark www.ibm.com/e-business or call us today at 1 800 IBM 7080, extension NC32.



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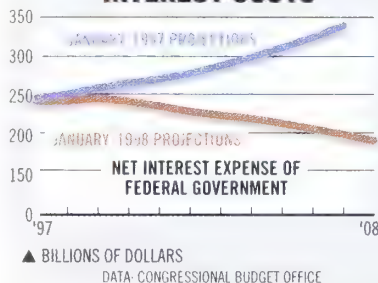
BY PETER COY

THE DEFICIT'S VIRTUOUS CIRCLE

As it shrinks, interest is trimmed

Rising budget deficits trigger a vicious circle. They increase the federal debt, so interest expenses on the debt go up, making the deficit balloon even more. As recently as last year, the Congressional Budget Office was projecting increases in the federal debt—and in interest expenses—as far out as it could see, namely until 2007. But with the ink in the federal budget turning

SCALING DOWN INTEREST COSTS



from red to black, the budget office sees the vicious circle changing into a virtuous one—a shrinking debt will mean steadily dropping interest payments, which will help cut the debt and make interest payments even smaller.

In fact, interest expenses could decline from 15% of the federal budget now to just 8% by 2008, according to the CBO. The result would be higher domestic investment, reduced current-account deficits, or both, says Prudential Securities Inc. Chief Economist Richard D. Rippe. And although the CBO assumes stable interest rates, Rippe says rates should fall—taking yet another bite out of debt-service costs.

WHY FREE TRADE WON'T HURT

U.S. jobs aren't lost, a study says

Fears that U.S. multinationals will move factories and jobs abroad have helped to derail the Clinton Administration's efforts to expand the North American Free Trade Agreement south to Latin America. Now, U.S.-based

multinationals are stepping up their counterattack with a study showing the domestic share of employment among U.S.-based multinationals has held steady at around 74% for 20 years.

The study, an analysis of Commerce Dept. data by Dartmouth College economist Matthew J. Slaughter, doesn't examine the impact of trade on overall employment patterns within countries, only on the multinationals themselves. It finds that total parent-company employment in the U.S. remained around 19 million from 1977 to 1994, while the employment of the companies in other countries actually declined from 7 million to 6.7 million.

Despite suspicion that multinationals seek mainly low-wage workers in less-developed countries, the study shows that nearly two-thirds of the overseas employees were in developed countries. Some 67% of total sales by foreign affiliates remained within the host country, and only 10% returned to the U.S. (The rest went to third countries.) The pattern indicates that sales, not wages, have been the principal motivation for establishing foreign affiliates.

By Paul Magnusson

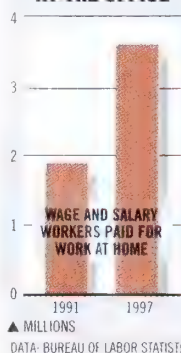
HOME SWEET OFFICE

At-home workers are on the rise

Working at home for pay has turned out to be one of the hottest employment trends of the 1990s. Between 1991 and 1997, the number of wage and salary workers who received pay for work at home nearly doubled, from 1.9 million to 3.6 million, the Bureau of Labor Statistics announced this month. Some 88% of those workers were in white-collar occupations, and they averaged nearly 15 hours of work at home each week.

Bureau economist William G. Deming speculated that an increase in corporate telecommuting programs may explain much of the increase. One hint that may be true is that there was not a corresponding increase in unpaid work done at home. Indeed, there was a de-

NO-SHOWS AT THE OFFICE



crease in the number of wage and salary workers who do work at home for which they are not paid, to 11.1 million from 12.2 million. Of those, some 2.8 million were teachers. In addition, roughly 6 million self-employed people do some work at home.

A WAY TO BEAT THE BANK

Check processing goes self-service

The U.S. has the world's most efficient financial system—and it got that way because competition prevented financial institutions from charging prices that are out of line with the costs. The latest case in point: A startup in Mobile, Ala., has come up with a strategy for stripping away banks' substantial profits from check processing. Innovative Treasury Systems Inc. shows grocery store chains how they can save money by processing customers' checks in-house instead of paying banks to do it. For a grocery chain with \$1 billion in annual revenue—say a little more than 100 stores—the savings can be \$600,000 to \$1 million a year, claims Roy W. Henderson, the company's executive vice-president for sales. Much of the savings come from capturing "float"—interest on funds that banks aren't crediting to the supermarkets as quickly as they could, he says.

Innovative Treasury Systems plans to branch out to other businesses that get lots of checks, such as utilities. Banks may be forced to lower their check-processing fees drastically in response, says Craig R. Macdonald, research director for World Research Advisory Inc., a Reston (Va.) financial consulting firm.

Innovative's concept involves regulatory finesse. The supermarket chain becomes a customer of its own employee credit union, which then serves as the chain's go-between with the Federal Reserve. That requires a dispensation from the National Credit Union Administration—ordinarily, businesses are not permitted to be customers of credit unions. American Bankers Association lobbyist James D. McLaughlin said he had not known of the concept, but called it "one more reason why we need credit-union legislation." Henderson says that if the credit-union route is blocked, customers could undoubtedly find some bank willing to be the intermediary with the Fed for a fee.

JAMES C. COOPER & KATHLEEN MADIGAN

SYMPTOMS OF THE ASIAN FLU ARE SHOWING UP

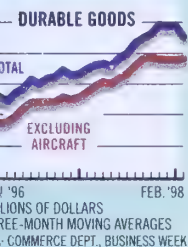
Trade and inventory buildup are flagging, and that can crimp growth

U.S. ECONOMY

Happy Birthday: The economic expansion of the 1990s turned seven in March. By historical standards, that's recent age, but this upturn still retains much of the vigor and bright prospects of its youth. Domestic demand is resilient, and the financial markets are booming, as low inflation keeps the Federal Reserve on the sidelines.

But as the expansion begins its eighth year, at least some areas are crucial to the outlook: foreign trade and inventories. Their swings can be volatile, and they can substantially influence overall growth. In the fourth quarter of 1997, for example, a huge inventory buildup added nearly 1½ percentage points to real gross domestic product growth. And in the first quarter, the deficit widened sharply, possibly subtracting as much as two percentage points from GDP growth.

THE SLOWDOWN IN FACTORY ORDERS



manufacturers' orders (chart).

Even so, the stellar performance of U.S. consumer spending and housing, buoyed by rising buying power, strong job prospects, and low interest rates, suggests that overall GDP grew about 3% in the first quarter. In January, sales of existing single-family homes soared 8.7% in January, to a record annual rate of 4.75 million. At the same time, inflation remains tame. But amid such strong domestic demand, the latest data on consumer spending suggest keeping a wary eye on service inflation, which is largely immune to the Asian flu.

EXPORTS, IMPORTS,

and manufacturing may have a lot to do with it, though. Foreign trade began 1998 flat on its feet. The January deficit for goods and services widened to a larger-than-expected \$12 billion, from \$9 billion in December. Imports slipped 1%, to \$89.3 billion, but exports fell by a bigger 2.6% to \$72.3 billion. However, the January trade data require a careful reading. First, the export drop was exaggerated. Fewer

shipments of aircraft, mainly from Boeing Co., accounted for 85% of the goods decline. Boeing delivered 16 planes to non-U.S. markets in January, down from 26 in December. But Asia was not a factor. Two Asia-bound planes were delayed but will be shipped later, the company said, and the rest of the decline was in line with normal monthly swings.

Aircraft shipments in the first two months of a quarter are often lower than those in the final month, Boeing says. Indeed, February foreign shipments dipped to 14 planes. But based on Boeing's overall first-quarter goal, March shipments probably picked up.

To be sure, export growth has slowed—even services. Exports such as finance, tourism, and royalty fees are expanding more slowly than they did a year ago (chart). While service exports are not reported by region, a chunk of the slowdown likely can be traced to Asia. Still, the falloff in exports to the Pacific Rim countries is not as dramatic as the latest data suggest.

THE EXPORT SLUMP IS HITTING SERVICES, TOO



FOR EXAMPLE, SHIPMENTS

of goods to the region, including Japan, China, and Australia, as well as the newly industrializing nations, plunged 12.9% in January from December. But that's similar to the trend of the previous five Januarys—before the crisis—when exports fell by an average of nearly 10%. The Commerce Dept. does not seasonally adjust the regional data, but BUSINESS WEEK's adjustment found that January exports to the Pacific Rim fell about 3%.

But even the overall data, which Commerce does seasonally adjust, may not tell the real story. In each of the last five years, net exports—the trade balance figure used in the GDP data—have narrowed in the fourth quarter, only to widen in the first quarter by an average of \$17 billion, despite Commerce's efforts to adjust for such recurring patterns. That's equivalent to a percentage point of GDP growth. The sharply wider January gap suggests that the trend continued in 1998.

The dollar value of exports has also been held down by declining export prices, which fell 0.7% in January and 0.2% in February. In the three months through January, exports of goods increased 9% from the year

before, but after price adjustments, the volume of shipments was up 15%. The steadily rising dollar should be making U.S. goods more expensive in foreign markets, but it appears that U.S. businesses are cutting prices in order to remain competitive, even if it means taking a hit to the bottom line.

Data quirks aside, it is clear that Asia's problems are now hitting U.S. manufacturers, who are rethinking production schedules. New orders for durable goods fell 1.7% in February, and first-quarter orders are running below their fourth-quarter average. February unfilled orders also fell, but they are still at a high level, suggesting that there is enough demand for U.S. goods to buoy output. Businesses are also adjusting their inventory levels. After the big runup in stockpiles in the fourth quarter, companies did not add to their inventories at all in January. And any gains in coming months are likely to be small. Slower inventory accumulation will subtract from GDP growth.

THE FOREIGN SECTOR is also having an impact on the inflation outlook. In February, consumer prices for all goods and services rose 0.1%, and they are up just 1.4% from the year before. A 2.2% drop in energy prices offset increases in other sectors. But even excluding energy and food costs, the core index has risen 2.3% over the past 12 months.

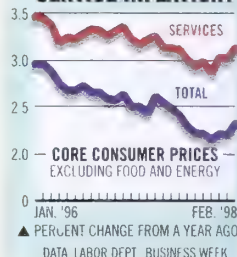
Falling import prices are one reason for the inflation

slowdown. In the year through February, prices of imported goods have dropped 6.1%, led by the plunge in oil prices. Moreover, the drop in prices of Asian goods is becoming steeper. The Asian-related deflation in prices of oil and other commodities will help to hold down goods inflation in coming months.

The outlook for service inflation, though, is a bit different. In February, core service prices rose 0.3% from January and 3.1% from a year ago. That rate is pretty modest, but it is up from 2.9% in November after a steady decline (chart). Bigger increases in the cost of shelter plus an upturn in medical services may be signaling that the disinflation in services is ending. And because service wages are rising 4.1% so far in the first quarter, service companies will probably feel more pressure to raise prices.

Any upturn in service inflation will not be dramatic or quick. And as long as lower goods inflation offsets some of the increase on the service side, overall core inflation will remain below 3% this year, although above 1997's 2.2%. Indeed, given the expansion's age and the current strength of domestic demand, inflation's remarkable quiescence will be difficult to maintain.

A YELLOW FLAG FROM SERVICE INFLATION?



ISRAEL

NO LETUP IN THE INFLATION FIGHT

Inflation may be the lowest in 28 years, but the Bank of Israel is not ready to abandon its tight monetary policy, even with the economy slowing sharply and unemployment rising. The central bank believes that Israel has the first chance in decades to bring inflation down to Western levels, and it knows rapid cuts in interest rates could hamper that goal.

The central bank did lower its key discount rate by 0.4 percentage point on Mar. 23 to 12.2%, the third cut in the past three months. However, since annual inflation is running at 5.6% in February, down from nearly 13% in mid-1996 (chart), real interest rates are still sky-high. In fact,

because of several temporary factors, such as falling food prices, the consumer price index actually declined in four of the past six months. In addition to tight monetary policy, fiscal restraint, falling commodity prices, and the Asian crisis have also helped to restrain inflation.

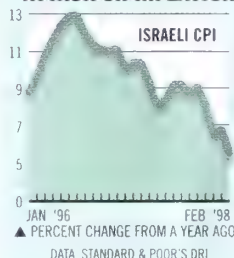
Since inflation is widely expected to slip below 5% for the year, further rate cuts are likely, but they will come gradually. Bank of Israel Governor Jacob A. Frenkel believes that it's too early to declare victory in the battle against inflation. His stated objective is to achieve price stability gradually over time, and his policies have won the praise of the International

Monetary Fund. The IMF also has called on the government to continue cutting its budget deficit, which at 2.4% of gross domestic product last year, was ahead of target.

However, many leading economists argue that the central bank's total focus on inflation is partially responsible for the deepening economic slowdown. After averaging 6% growth in the first half of the 1990s, Israel's GDP slowed to 4.5% in 1996 and to only 2.1% last year. For 1998, analysts project growth of no more than 2%. As a result, unemployment has risen from 6% in the second quarter of 1996 to 8% at the end of last year, and it is set to climb further. The fear is that Frenkel's likely victory over inflation will cost the economy dearly.

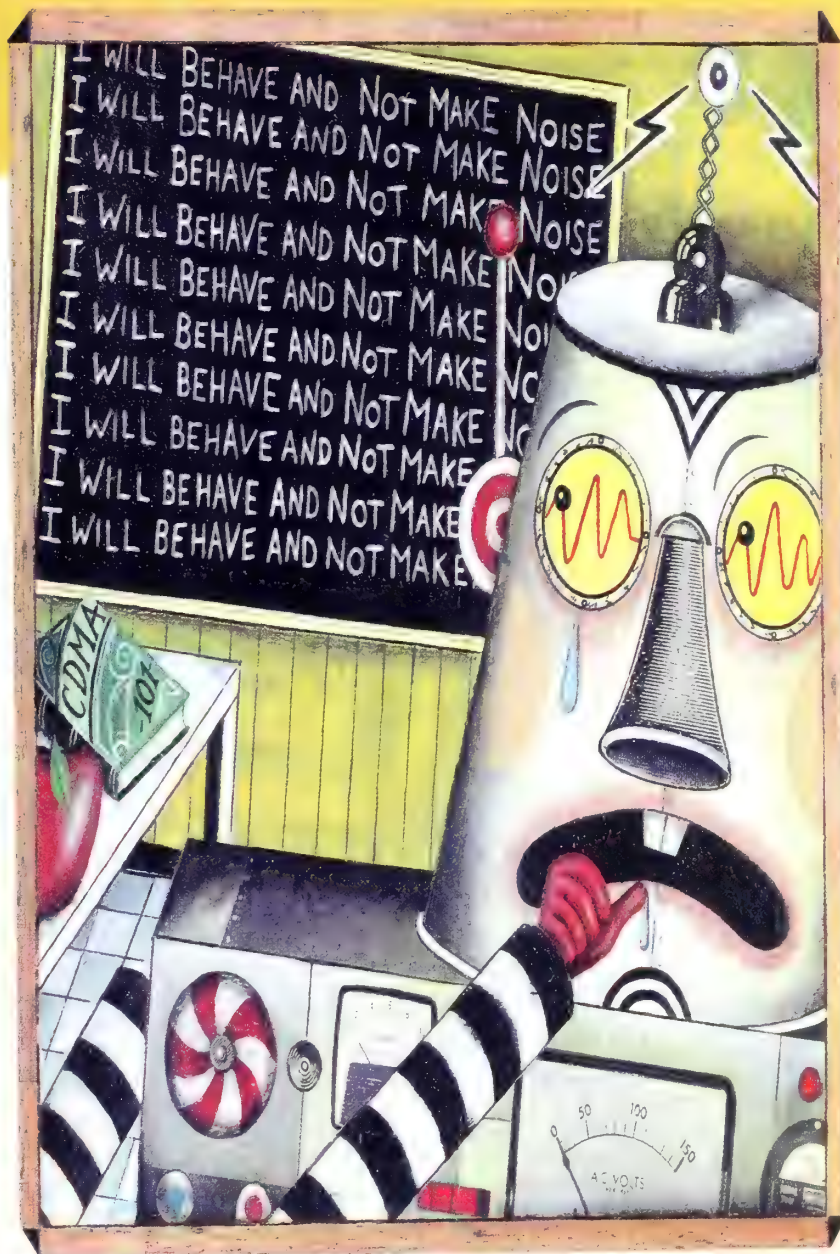
By Neal Sandler in Jerusalem

THE CENTRAL BANK'S ATTACK ON INFLATION



NOW THAT WE'VE DISCIPLINED TECHNOLOGY, IT'S READY TO LISTEN TO YOU.

ut guidance, wireless technology acts like
d but mischievous child who makes noise
ngs up your calls. Now with our instruction,
rned control. QUALCOMM digital phones
ou crystal clear conversations without
ramental sound quality. And because it's
nger disruptive, it won't interfere while
alking. It's actually our CDMA technology
romotes good behavior by providing high
quality and enhanced security to guard
st cloning and fraud. Now that we've
d wireless technology, it's more than
boisterous youngster only a mother
love. For more information, visit us at
qualcomm.com/quiet or call 1-800-349-4188
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DIGITAL PHONES

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Provider options may vary. CDMA voice quality rated superior by 1997 TRAC Study.

Norma Madison has had it with her cable-TV company. The 64-year-old retired deli clerk lives on less than \$500 a month in rural Springfield, Ore. Yet she forks over \$43.62 for basic television reception—more than double the \$18.80 she paid in 1990. “They’re pricing people right out of TV,” she says. And what’s she getting for her money? “The John Wayne and Clint Eastwood films have been rerun at least 30 times each,” she says.

Madison is ready for a shoot-'em-up—and she's not alone. Consumers are livid about cable rates, which rose 8.5% on average last year, four times the inflation rate. So with elections looming, pols and policymakers are coming out with guns blazing. They have an opening: The Federal Communications Commission's authority to regulate cable rates expires in March, 1999. “We shouldn't expose consumers to an unregulated monopoly,” says FCC Chairman William E. Kennard, who wants Congress to consider renewing the FCC's powers.

The cable crisis is another sign that the 1996 Telecommunications Act hasn't lived up to its promise. When the Act passed, lawmakers had expected cable competition to spring up from local phone companies and from satellite. Instead, phone companies have been plowing money into new capacity and better data-communications services. And high costs have kept operators of direct broadcast satellite (DBS) systems from grabbing big chunks of the market from cable. “Waiting for competition has been like waiting for Godot,” says Larry Irving, assistant secretary at the Commerce Dept.

LEG UP. Congress isn't considering re-opening the telecom act—yet. But if cable rate rises don't subside, House Republicans want to introduce “video competition” legislation by 2000 to help cable's rivals. Other proposals range from reregulating rates to giving rivals such as DBS operators a leg up. Representative Peter A. DeFazio (D-Ore.) has even proposed freezing cable rates.

First, though, Congress must decide whether to extend the FCC's authority to

CLIPPING CABLE'S POWER

As rates rise,
viewers and
rivals gripe—and
the pols mull
the options

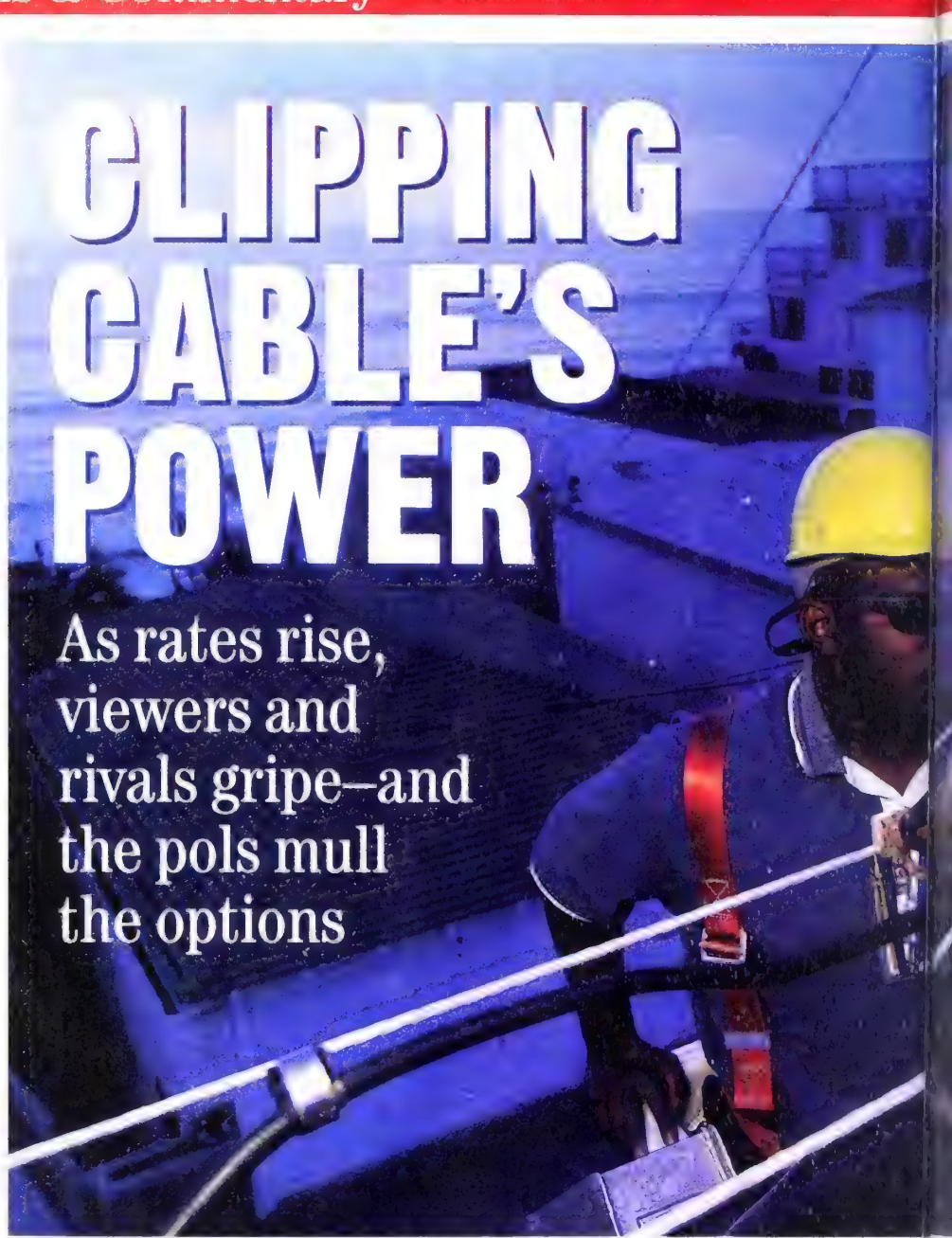
regulate the industry. While Representative Edward J. Markey (D-Mass.) has already introduced a bill to do that, Republicans are balking.

The GOP has its own preferred route: Aid satellite TV rivals by lowering the copyright fees they pay to carry network broadcasts, allowing them to transmit local broadcasts and giving them better access to cable programming. “If competition hasn't emerged, we've got to do more than let cable companies continue,” says House Telecommunications Subcommittee Chairman W.J. “Billy” Tauzin (R-La.).

The cable industry insists there's no need for new regulations and point to continuing subscriber growth as a sign

that consumers aren't unhappy. Telecommunications Inc., in Englewood, Colo., gained 155,000 new subscribers in the last quarter despite rates that are 6.5% higher than a year ago. And on Mar. 2, TCI reported a 28% jump in operating cash flow for its latest quarter. Englewood (Colo.)-based Media One saw a 2% rise in subscribers after raising rates 8% in January. Consumers “feel they are getting service for the money,” says Executive Vice-President Ron Cooper.

They can expect to pay even more. Under current rules, cable operators can pass along most cost increases to ratepayers. The biggest variable now is the soaring price of programming. The Knicks want to sign Michael Jo-



WHAT CONGRESS COULD DO

COPYRIGHT FEES

The House and Senate are considering bills to give direct broadcast satellite providers a break on copyright fees to transmit network programs.

LOCAL-TO-LOCAL TRANSMISSION

Senator John McCain (R-Ariz.) plans to introduce legislation to allow DBS companies to transmit local broadcast signals in local markets.

PROGRAM ACCESS

Lawmakers could stiffen rules requiring cable operators to offer programs to rivals at fair prices.

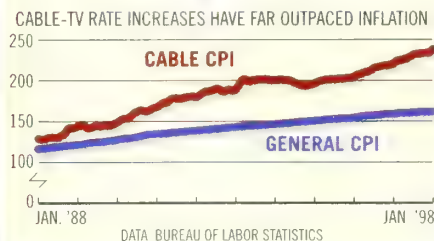
RE-REGULATION

Representative Edward Markey (D-Mass.) has introduced legislation to extend the Federal Communications Commission's cable-rate regulatory authority beyond Mar. 31, 1999.

VIDEO-COMPETITION LEGISLATION

House Republicans may consider legislation to promote competition by DBS if cable rate hikes continue.

ZAPPING CUSTOMERS



HER WIRE: dan for \$50 million a year, guess who gets to pay for it?" asks John Malone, chairman of TCI, which says its programming costs 70% of costs. "The poor cable subscriber and their poor cable operator."

Cable companies also are asking customers to help pay for network upgrades. Operators spent \$7.5 billion to and improve systems and services, only the same proportion of revenues as the telcos spent, says Bank America Robertson Stephens analyst Andy Horan. By 2000, with high-cable wiring, new switching equipment,

digital set-top boxes, and cable modems, the cable systems may offer competition to local telcos. "The FCC has got to look at this from a more holistic point of view," says Bob Fox, vice-president at Mercer Management Consulting.

Holistic, schmolistic, counters the FCC, which doesn't believe the industry has to charge consumers for future improvements. Cable operators enjoyed cash flow estimated at \$12 billion last year, up from \$9.7 billion in 1992, according to Paul Kagan Associates. Ad revenues jumped 12%, to an estimated \$1.9 billion over the last year, says Kagan.

In contrast, cable's DBS rivals still lag badly. DBS operators have just 6.9% of the pay-TV market, compared with ca-

ble's 87%. Potential customers have been turning down DBS, largely because it doesn't carry local channels. Senate Commerce Committee Chairman John McCain (R-Ariz.) plans to introduce a bill changing that in April.

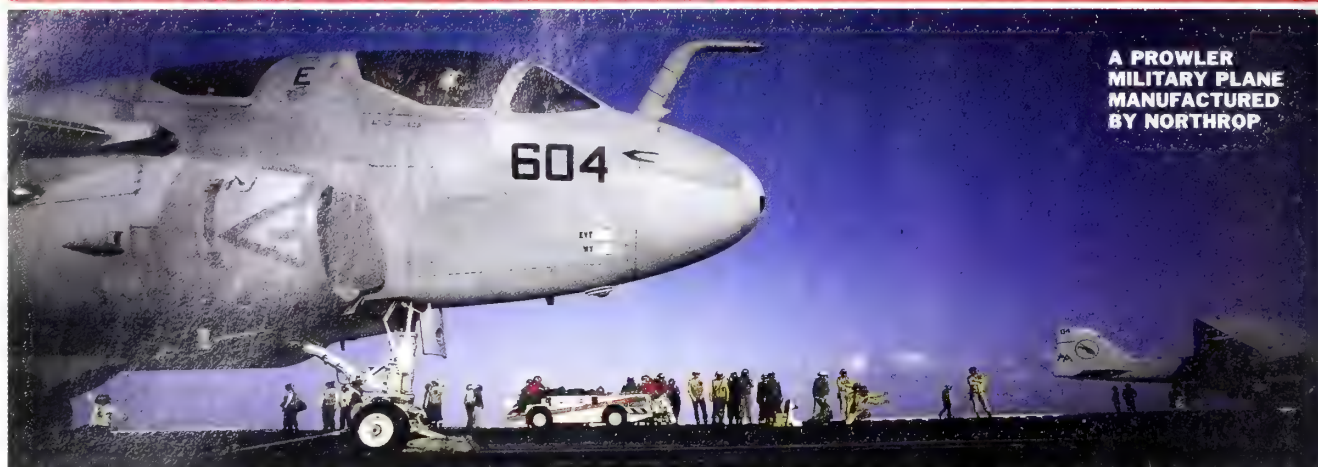
Satellite operators also want Congress to strengthen rules requiring cable companies to provide programming to rivals on fair terms. DBS companies say they often are forced to pay a premium. "We shouldn't have to pay more," says Charles W. Ergen, CEO of EchoStar Communications Corp.

Direct broadcasters also complain about programming access. Cable companies that own programmers and transmit via satellite are required to sell programs to all comers on an equal basis. But cable companies try to work around that rule. In September, DirecTV filed a complaint at the FCC against Comcast Corp. for refusing to let it carry Comcast SportsNet. Comcast is delivering the programming via a fiber-optic network and says it does not have to follow the satellite program-access rules.

NO SWEAT. Cable competitors want the Justice Dept. and the FCC to block a merger between American Sky Broadcasting Co., which is News Corp.'s U.S. satellite property, and Primestar, a satellite broadcaster owned by a cable consortium. The combination would concentrate "a disproportionate share of the precious spectrum" that is supposed to compete with cable, says DirecTV President Eddy W. Hartenstein.

For now, the cable industry isn't sweating. "I am very optimistic," says Leo J. Hindery Jr., president of TCI. Still, the cable guys can't be too complacent. "The cable companies claim they don't act like monopolists," says Gene Kimelman, co-director of Consumers Union. "But all the while, they're charging prices like monopolists." As autumn draws nearer, both Democrats and Republicans in Washington could be outdoing themselves to find votes by taking on the local cable companies.

By Catherine Yang in Washington, with Ronald Grover in Denver and Steven V. Brull in Los Angeles



A PROWLER MILITARY PLANE MANUFACTURED BY NORTHROP

TRUSTBUSTERS

HOW LOCKHEED'S EARLY-WARNING SYSTEM CRASHED

It misread Justice's growing alarm with defense mergers

If only former Lockheed Martin Chief Executive Norman R. Augustine had followed his own advice when he sealed the deal to buy Northrop Grumman Corp. for \$11.6 billion last July. Only five months earlier, he had written in an aerospace trade publication that the government should have a "great deal of concern" about prime contractors gobbling up suppliers. And while he and his successor, Vance D. Coffman, may have ignored it, a Pentagon task force studying defense mergers hadn't. It quoted Augustine in a May report warning of the dangers of such vertical integration. "We basically spelled out for Lockheed Martin that any future mergers would not be welcome," recalls task force member Carol V. Evans, a Georgetown University professor.

"FULL-BLOODED COMPETITION." Lockheed is now paying a huge price for its lapse. On Mar. 23, the Justice Dept.—egged on by the Pentagon—sued to block the planned merger with Northrop. Justice argued that the new combo would create monopolies in electronics hardware such as airborne early-warning radar. Worse, the merger would enable Lockheed Martin to rely on its own inhouse parts suppliers and snub rivals. "Our nation cannot afford anything less than full-blooded competition," Attorney General Janet Reno declared.

So how did Lockheed miss all the obvious antitrust warning signs? Two years ago, the government began to grow queasy about the dwindling num-

ber of critical arms makers as leading suppliers paired off in mergers, consolidating in a post-cold war world. After Washington approved Raytheon Co.'s purchase of Texas Instruments Inc.'s defense electronics division in 1997, Justice antitrust chief Joel Klein told Congress that future mergers would get close scrutiny. But while the government saw too much concentration, Lockheed Martin saw only the need to expand in size so it could compete with the expanded Raytheon.

In round after round of negotiations, the players ended up talking past each other. The government consistently raised concerns about the merger, but Lockheed Martin believed that it could ease antitrust concerns by spinning off some units or agreeing to a consent decree that would require it to seek outside bids for sub-contract work.

Only on Mar. 6, months after the negotiations began, did the Lockheed brass realize their error. The Justice Dept. and the Pentagon dropped a bomb: The merger as planned would not be approved. To satisfy Justice, Lockheed Martin would have to divest \$4 billion in the electronics business, far more than the \$1 billion that Lockheed Martin thought necessary. Lockheed's

and Northrop's response was predictable: The government's demand "undermine the economic viability of the transaction," the companies said in a joint statement.

Could this marriage have been saved? Analysts doubt there was much Lockheed Martin and Northrop Grumman could have done. "Timing is everything," says Andrew F. Krepinevich, executive director of the Center for Strategic & Budgetary Analysis. "They just showed up at the consolidation party one round too late."

For now, Lockheed Martin is mulling a variety of responses, from a new structure for the deal to a court fight to unblock the merger. It will argue that divestitures can solve the monopoly concerns. What's more, the combined company would still be a smaller military aircraft maker than Boeing Co. and smaller electronics supplier than Raytheon. The government would end up with two strong competitors in each arena, rather than one strong and two weak ones. The company will argue in court. Lockheed Martin also plans to claim that its record shows it doesn't favor inhouse suppliers. But its argument may be weakened by a recent suit brought against Boeing by Teledyne Ryan Aeronautical, a former supplier. It claims McDonnell Douglas, now a part of Boeing, breached a contract to buy airframes for the Apache helicopter and gave the work to a Boeing unit.

But antitrust experts doubt any Lockheed Martin's arguments will work now. That makes former CEO Augustine prescient—painfully so.

By Stan Crock, with Susan Garland in Washington



CROSSED SIGNALS?

CEO Coffman, a Beltway newcomer, thought spin-offs might allay fears

By Paul Magnusson & Dean Foust

DON'T WASTE A HUGE OPPORTUNITY IN AFRICA

Finally, it's Africa's turn. As President Clinton told a massive crowd in Ghana on the first leg of his six-nation tour on Mar. 23, "It is time for Americans to put a new Africa on our map." He wants the U.S. to take the lead in helping Africa plot a new path—toward democracy, market reform, and self-reliance.

Cynics view Clinton's 12-day visit—the first by a U.S. President since Jimmy Carter—as a welcome diversion from his personal scandals.

FRIENDLY HAND

Bill Clinton is shaded by Ugandan First Lady Janet Museveni as President Museveni looks on

But it can be far more. The trip is a belated recognition of the vast potential of Africa, a continent that in the post-cold war era no longer has to be a battleground between capitalism and communism. The new models are Botswana, with a two-party democracy and a 5.5% growth rate. Or Ghana, which has modernized its phone, electric, and road systems while privatizing gold mines. In Uganda, growth is running above 6%, thanks to market reforms.

Further progress depends on expanded trade and investment, areas on which the Clinton Administration wisely plans to focus. But unless the U.S. Senate passes a bipartisan economic stimulus package for the continent, Clinton's trip will be in vain.

ALL IN OIL. While still relatively minuscule, trade between the U.S. and the 48 nations of sub-Saharan Africa grew at the same 32% rate as trade with the rest of the world over the past three years. And although Africa accounts for just 1% of America's exports and 2% of its imports, the U.S. is Africa's leading market, purchasing 19% of exports since 1994. Unfortunately, 90% of U.S. purchases from Africa involve oil, which provides less economic pay-back than manufactured goods.

Africa, for example, gets little out of U.S. programs that grant duty-free

treatment to manufactured products from developing nations. "Foreign aid alone has not led to the kinds of growth and diversification that increased trade would produce," says U.S. Trade Representative Charlene Barshefsky.

The Administration supports a House-passed trade bill called the Africa Growth & Opportunity Act, which would grant further preferences for textiles and clothing in return for market reforms. But the bill faces opposition because it could cost

for example, recently endorsed a new business plan for the region that foresees 15% growth rates. Today, Africa accounts for 7% of the company's customers but only 4% of sales. "We see an Africa more directly accountable for its own destiny than it has been for centuries," Coke CEO M. Douglas Ivester said recently.

CIVIL STRIFE. Africa still has enormous problems, including a crumbling infrastructure, endemic corruption, and civil wars. Market economies are just taking hold in for-



jobs in a U.S. apparel industry that has already been hit hard by competition from abroad. Even so, the measure would just hasten the inevitable: Protective import quotas on textiles are scheduled to be phased out by 2005. The U.S. International Trade Commission, an independent agency, notes that further domestic job losses would be minimal, since Africa accounts for less than 1% of U.S. textile imports.

The trade bill would also allow duty-free zones in countries that are making progress in moving toward a market economy and improving human rights. It would establish two funds to invest \$650 million in African business and infrastructure and order the Export-Import Bank to expand loans, guarantees, and insurance to Africa.

More important, the bill would help highlight the continent as an investment opportunity. Coca-Cola Co.,

merly socialist nations such as Tanzania, and decades of mismanagement have wrecked the economy of the Democratic Republic of Congo (formerly Zaire). Protracted internal conflicts have ruined the neighboring nation of Republic of the Congo as well as Burundi and Sudan. Nigeria is widely considered one of the most corrupt nations in the world.

But these problems also create huge opportunities for improvement: A recent Transportation Dept. study notes that a dollar invested in the African transportation grid would likely return more than a dollar in increased economic activity every year. Indeed, Africa is ready for a new kind of exploration that will benefit investors, traders, and 750 million inhabitants.

Magnusson covers trade and Foust covers international economics from Washington.

WASHINGTON

NEWT GINGRICH'S 'GOALS FOR A GENERATION'

The Speaker discusses his plans for the GOP and the White House

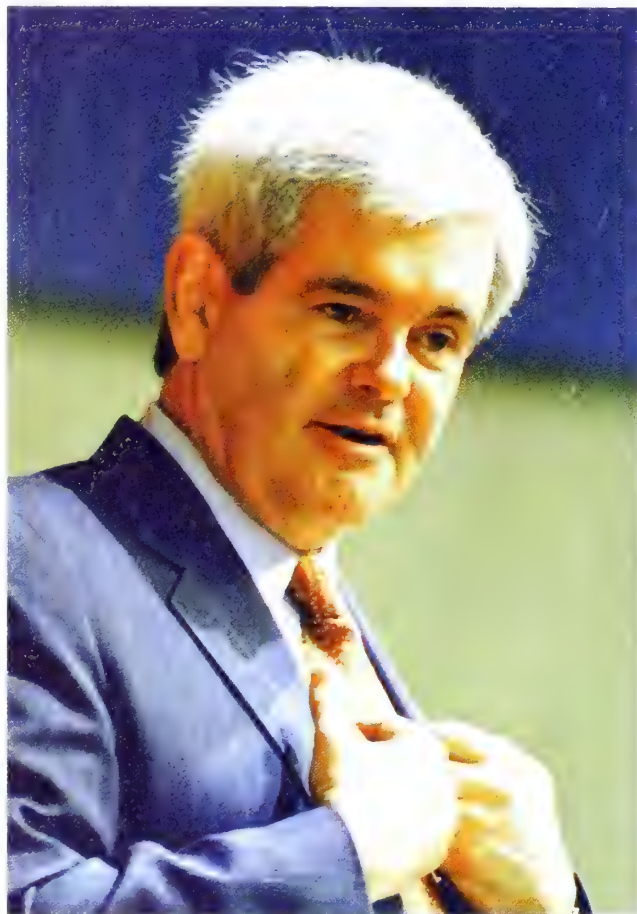
Newt Gingrich is in the midst of the latest of the many metamorphoses that have marked his controversial career. After surviving a palace revolt that nearly cost him his leadership post last July, the House Speaker has ended a self-described period of introspection. His aim now: to reassert his role as the GOP's chief idea merchant and preserve the party's slim House majority this fall while presenting himself as a kinder, more moderate leader. "A year ago, the question about Newt was: 'Will he survive the week?'" says former Reagan Chief of Staff Kenneth M. Duberstein. "The question now is: 'Will he run for President?'"

Gingrich has more immediate concerns. To save the House from a determined Democratic charge, he has adopted a frenetic fund-raising schedule that has pulled in more than \$40 million since January '97. Gingrich also aims to retool his party's platform for '98 and beyond. He's urging the GOP to rally around four goals: capping the total state, federal, and local tax burden at 25%, fixing Social Security, improving education with incentives for teacher quality and school choice, and intensifying the war on drugs.

Gingrich's agenda shows how much he has evolved in three years. After continually being clobbered by Democrats for appearing hostile to kids and seniors, the new Newt feels compelled to offer new policies on such issues. And by focusing on a lighter tax bill for all, he's trying to insulate the GOP from charges of pandering to the rich.

How is Newt's new act playing? He has a way to go before he's considered cuddly. Since the failed coup, his Harris Poll favorable rating has gone from a measly 23% to a so-so 36%. Only someone as self-assured as Gingrich would consider that enough to daydream about the White House. "Newt's a polarizing politician," says GOP adviser Wayne Berman. "But he knows that polarizing politicians, such as Nixon and Reagan, can win if they lay the groundwork."

On Mar. 25, Gingrich sat down with Washington bureau chief Lee Walczak and correspondent Richard S. Dunham to discuss his initiatives—including his Presidential plans.



Q: President Clinton has co-opted core GOP issues such as a balanced budget and welfare reform. Are there any big new ideas for Republicans to push?

A: I've been describing four Goals for a Generation. I expect Clinton to coopt as much of them as his Left will permit. The first is a drug-free country with a dramatic decline in crime. The second is a world-class education and learning system. The third is to use [budget] surpluses to guarantee Social Security. The fourth is to reduce the tax burden from 38%, on average, to 25%. I think you have a very decisive platform for Republicans, not just for '98 but for 2000.

Q: Don't polls show that tax cuts are far from most Americans' minds right now?

A: I'm creating a vision-level goal here. I'd be glad to have Al Gore run [for

President] as the higher-tax, bigger-government, please-pay-for-more-bureaucrats candidate.

Q: Do you favor a flat tax or the rival plan for a national consumption levy?

A: Let me be straight about this. No Republican should pick one of those two before 2001. Because liberals will pick every defect in whichever one you choose and beat you brains out.

Q: Many business leaders think it's irresponsible for the House to hold up a funding bill for the International Monetary Fund over abortion restrictions. Your response?

A: Why is it that Bill Clinton can say no IMF money because we have to support \$1 million for organizations to lobby in favor of abortion overseas? Somehow, that doesn't make him an extremist. So I say to all of my business friends: Go talk to the President.

Q: Are Republicans losing their enthusiasm for free trade?

A: There is mythology out there. It comes back to Pat Buchanan's ['96] campaign. We had 16 votes out of 228 for

“ [I'd run] if I was drafted for the nomination. That'd be ideal. Hasn't happened in modern times ”

fast-track. That was a higher percentage than we had for NAFTA. This is a very international, world-market party.

Q: Is there merit to the Administration's aggressive antitrust push?

A: All the prosecutorial energy in the

e Dept. has been put into one nar-
one. I had breakfast with [Micro-
CEO] Bill Gates about two years
and he said: "You know, I'm either
next monopoly or I'm bankrupt." If
think about IBM, AT&T, and General
ers, I'm not certain that an 1890
-state model based on natural mo-
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very dubious about the settlement.
a are not going to protect DuPont,
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x collector of the Nanny State."
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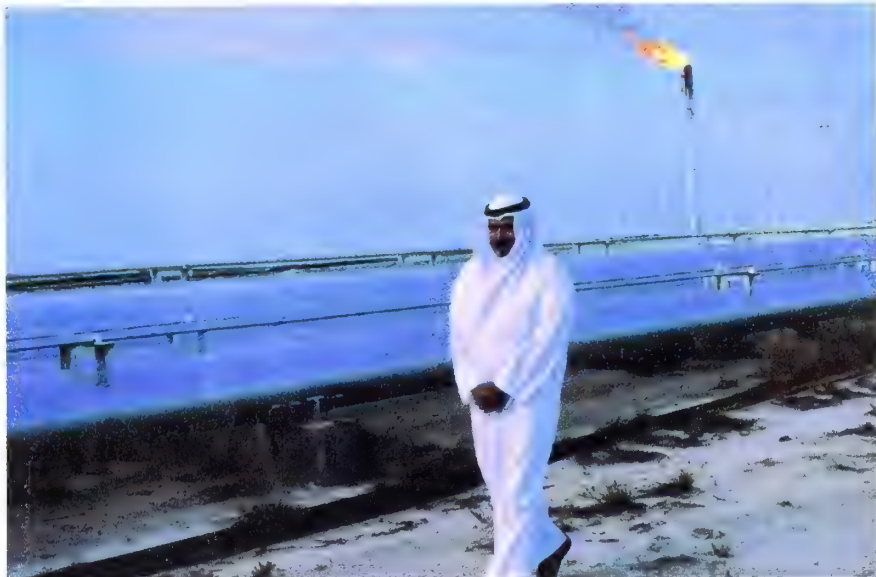
ey must have been talking about
tel Majority Leader] Trent Lott.
et used to it. You have the same
on that Lincoln did. You learn that
friends have very high standards,
what you've got to do is listen to
carefully and do what you think is
—and not worry about it.

ome of your advisers think you're
g the groundwork for a Presidential
aign. What would make you run?
(smiling) Well, one is if I was draft-
r the nomination. That'd be ideal.
t happened in modern times. Being
gorgian, I can't issue a Sherman-
statement. I will not think about
opic until late '99.

n polls, most Americans say the
dent's sexual conduct isn't grounds
npeachment. Yet you're preparing
npeachment proceedings. Could
backfire?

o. We're not going to do anything
s [Independent Counsel Kenneth]
does something. I suspect he'll de-
a bunch of evidence to the country.
is relevant to whether or not the
of law has been violated, we'll act.
isn't, we won't.

n extended version of this interview go to
America Online: Keyword: BW or
www.businessweek.com.



ENERGY

SQUEEZING THE PIPELINE

Oil producers strike a deal that lowers prices—for now

And now we return to *As the Oil Market Turns*. In our last episode, finances of OPEC nations were sinking in a pool of excess oil. Then, on Mar. 22, Saudi Arabia managed to persuade fellow OPECer Venezuela and Mexico, not a member of the oil cartel, to curb production. According to the revised script, the trio will chop output by a combined 600,000 barrels a day, to begin with. But "we will surely reach the amount of 1.6 million to 2 million barrels a day," Venezuela Energy Minister Erwin Arrieta enthusiastically pledged. News of the proposed cutbacks reversed a four-month plunge in the price of crude, sending oil up nearly \$2 a barrel.

But, dear listener, that's not the end of our story. Will the cutbacks really halt the plunge? Can OPEC enforce a reduction this time—a feat it has not pulled off since 1986? Could the fragile agreement be dashed by Iraq's pending U.N. oil-for-aid sales?

QUICK FIX. Count on months of intrigue ahead. In the short term, the deal may stabilize the price of crude at about \$16 a barrel—up from its mid-March lows, but well below its 1997 average of \$21. "This is a short-term palliative," says PaineWebber Inc. oil-watcher Frank P. Knuettel. "They want prices back in the upper teens; it isn't going to happen with this agreement."

Indeed, crude settled at \$16.48 on

SHORING UP: The agreement could be too fragile to succeed in the long run

Mar. 25 as traders calculated a more likely reduction of 1 million to 1.2 million barrels a day rather than the threatened 2 million. While still significant, the reduction comes as a seasonal slowdown is beginning: Demand for heating oil is waning and the summer driving boom is months away. On Mar. 24, the American Petroleum Institute reported that U.S. stocks of crude oil hit 326 million barrels, 1.5% higher than a week earlier and up 7% from levels a year ago.

Getting prices to rise and stay at higher levels would require measures few big producers seem willing to accept. In the current agreement for production cutbacks, Iran consented to a sleight-of-hand that trims 140,000 barrels off a quota it isn't near to achieving. Saudi Arabia's decrease of 300,000 barrels a day is less than half the 760,000-barrel production increase it approved last November. Plus, Venezuela says it will keep expanding capacity even as it pledges to lower daily production to 3.2 million barrels for the rest of the year.

Still, there are strong reasons for the oil-dependent trio to hold the line. Shrinking income from oil is forcing Mexico to slice spending by \$3 billion, and Venezuela has chopped 6% off its government expenditures. Meanwhile, Iraq is poised to release up to 500,000 new barrels a day under the U.N.-orchestrated oil-for-aid program. "Longer term, that's going to keep the market from getting much above \$15.50 a barrel," says Sarah A. Emerson, director of petroleum analysis and price forecasting at Energy Security Analysis Inc. Unless a Mar. 30 emergency OPEC meeting produces lasting cutbacks. Stay tuned.

By Gary McWilliams in Houston, with bureau reports

SOFTWARE

MICROSOFT: LET'S NOT GET CARRIED AWAY

Sure, earnings are up—but growth won't come as easily in '98

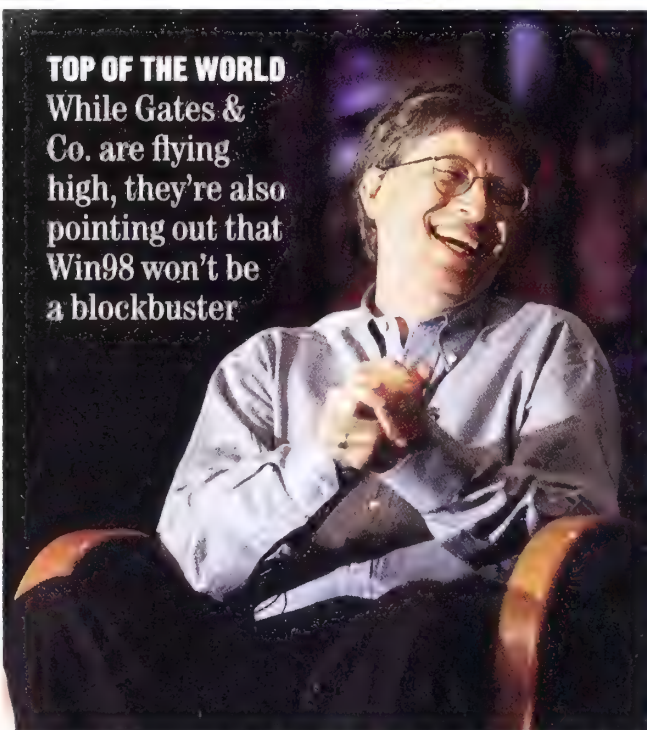
These days, when Wall Street gets a surprise from the high-tech sector, it's usually a nasty one—another warning of disappointing earnings from a computer maker struggling to turn a profit on sub-\$1,000 PCs or a diskmaker with inventory woes. No wonder that an upside surprise from Microsoft Corp. on Mar. 24 sent the software giant's shares soaring nearly 4 points to a record 88 $\frac{1}{2}$ ¢. Sales are so strong that the company issued a heads-up: Its earnings will beat analysts' expectations by 4¢ a share this quarter.

This will make it even harder for Microsoft to get analysts to pay attention to the other part of the message—the part about how sustaining such strong growth won't be easy. The company has warned repeatedly that its growth must inevitably slow. But just as routinely, Microsoft has continued to rack up double-digit gains. Sure enough, on Mar. 24, Chief Financial Officer Greg Maffei warned that the future doesn't necessarily look so rosy.

But this time, the warning may be apt. For starters, worldwide growth in PC shipments is slowing. More important, Microsoft faces uncertainty about the prospects for Windows 98, its only major product launch this year, and growing pressure from PC makers to lower prices. Most analysts agree with Maffei that, despite a massive Win98 marketing campaign that will begin in April, Microsoft won't head into a major new growth spurt until Windows NT 5.0, aimed at businesses, rolls out in early 1999. Michael Kwatinetz of Deutsche Morgan Grenfell Inc. has added only \$200 million to \$300 million to his revenue forecast over the next year for Windows 98 upgrades, which are expected to ship in June. That compares with a \$1.5 billion revenue boost the company got from Windows 95.

What gives? As Maffei notes, Windows 98 doesn't offer the attractions for

TOP OF THE WORLD
While Gates & Co. are flying high, they're also pointing out that Win98 won't be a blockbuster



consumers that Windows 95 did—a whole new look and major improvements in speed. Win98's main draws are integration of Microsoft Internet Explorer, which most consumers get already, and some new hardware-support features. "I don't see there's a huge, obvious marketing feature for consumers here," Maffei says.

Then there's the bruising price war in PCs. While Microsoft and other software makers are thriving, the average price for a consumer PC has dropped 36% in the past year. Microsoft has kept the price that PC makers pay for Windows steady in the low \$40s, according to analysts.

PC makers are lobbying for relief. "The margins have to be rebalanced," says Stan Shih, chairman of Acer Group Ltd. So far, however, there's no sign that Microsoft will go along. Says Maffei: "They're asking for price cuts? Sure. They

ask for cuts all the time. But we believe Windows provides a lot of value for them." Still, Microsoft has decided not to raise the price when it switches over to Win98.

Then there's the question that won't go away: Will the Justice Dept. halt shipments of Win98? Trustbusters might file an injunction to interrupt the product's shipment and force Microsoft to

offer a browser-free Win98.

Meanwhile, Microsoft is hesitant on shipping Win98 on time, if not early. On Mar. 10, it briefed PC makers and retailers on its game plan—including a May 18 target for sending the product to PC makers, according to a PC company source. As recently as February, Microsoft would promise only that Win98 would get to PC makers before the end of June. PC makers could be shipping by mid-June, and retail versions should be in stores by the end of that month.

AT THE MOVIES. Windows 98 marketing kicks off in earnest on Apr. 4—at a theater near you. The company has rented 38 movie houses from Normal, Ill., to Las Vegas for two-hour live broadcasts of demos of Win98 and other products. The audience: some 40,000 "computer enthusiasts"—buyers who are likely to upgrade in

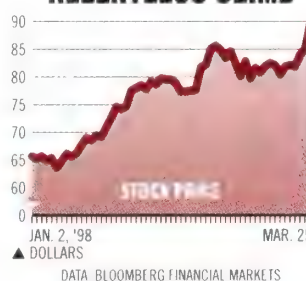
mediately and get friends and family to follow. "They're really the opinion leaders," says Ken Schneider, marketing director for Microsoft's consumer sales unit. Microsoft also will plug Win98 at its monthly "Family Technology Night" events at elementary schools around the country.

The formal marketing program is likely to stress co-marketing deals with peripherals makers: Easy connection via the so-called universal serial bus is one of Win98's most pluggable features.

By June, Microsoft's marketing engine will be at full roar—if Justice doesn't spoil the party. So by the time Microsoft brings in analysts for their annual summer briefing, we know whether Maffei was right, for once, when he warned investors to worry.

By Steve Hamm
San Mateo, Calif.

MICROSOFT STOCK'S RELENTLESS CLIMB



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By Robert D. Hof

JAVA CAN BE A CONTENDER—IF SUN LETS IT

Ever since Sun Microsystems Inc. invented Java, a computer language for creating programs that run on computer networks, Chief Executive Scott G. McNealy has boasted that it would roast Microsoft Corp. Now, it's Java that's getting roasted—and not just by the software giant. On Mar. 20, Java partner Hewlett-Packard Co. broke ranks. Accusing Sun of keeping too tight a rein on developing new versions of Java, HP has created its own Java variant for noncomputer devices such as printers. Meanwhile, other Java backers are muttering about Sun's heavy-handed stewardship of Java's evolution. Even avid Java programmers carp about its shortcomings.

Can McNealy keep Java perking? Yes, but only if he—along with Java partners and customers—quit their petty infighting. Java may never knock off Microsoft's Windows. But faults and all, Java is still an important breakthrough: A system for creating software that runs, unaltered, on all sorts of computers and devices. That could make doing business across the Internet simpler and could transform the software business in the network era from a one-horse race led by Microsoft to a true contest.

This all depends, however, on whether Java becomes a true standard. So far, McNealy's approach has been to insist on strict terms for other companies' use of "100% Pure Java" to enforce uniformity. When Microsoft developed a Windows-only version of Java, Sun sued for breach of contract and, on Mar. 24, the U.S. District Court in San Jose granted a preliminary injunction preventing Microsoft from using the Java logo.

Problem is, such victories may not help McNealy with his bigger goal—to make Java a widely used standard. Nor do his disparaging remarks about

Microsoft and its products do more than amuse geeky aficionados of Sun's Unix operating system. For Java to succeed, McNealy needs to befriend Windows programmers, not insult them. Says Stan Wang, CEO of Java startup Infospace: "We don't want to be in the middle of a holy war."

McNealy's energy and skill would be better spent in fixing the broken promises he has made to Java enthusiasts. Its shortcomings—bugs, primitive programming tools, and relatively slow performance—have allowed Microsoft to belittle the original and offer improvements tied to Windows.

gaps vexing them and other partners—and quell fears that Sun is shaping Java to benefit its \$8.5 billion computer business. "It would be a benefit to the whole industry," says Gary L. Steele, CEO of Java startup Netiva Software Inc.

STRONG START. A little cooperation would help, too. Java already is off to a strong start, running on 70 million PCs and other computers. But if more computer makers create more variants, that momentum will slow. That's why HP's split is shameful. HP CEO

Lewis E. Platt—whose company still backs Sun's Java for computers—should tell his managers to stick to

SPLAT! Gates will win again, if McNealy can't keep Java backers like Platt in the fold



As HP's defection shows, Java could splinter into incompatible camps—trashing its promise of programs that can "run everywhere." The situation is coming to resemble what happened a decade ago with Unix, another would-be universal standard: Each computer maker tweaked it, and soon programs had to be written anew for each brand—while Windows delivered guaranteed uniformity and became the overwhelming standard.

How to avoid a rerun? One bold step McNealy should consider: Cut loose Sun's JavaSoft unit that controls Java now. With adequate investment by partners such as IBM and Oracle Corp., JavaSoft could address the

what programmers want: the ability to write their programs once and run them anywhere. HP's move—backed by Microsoft—endangers that.

So far, "Java hasn't lost any momentum," says Goldman, Sachs & Co. analyst Laura Conigliaro. But in a business this fast-moving, customer perceptions are as important as reality. And the perception today is that Java is getting diluted. Unless Sun and its partners can wise up and start looking past their own noses, that perception could become reality. Then, it's game over: Bill Gates wins again.

Hof covers the computer industry from San Mateo, Calif.



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ASIAN TURMOIL

THE EARTH IS SHIFTING UNDER HEAVY EQUIPMENT

Cheap machines back from Asia could sink U.S. dealers

Only a year ago, Triad Machinery, a construction-equipment dealership in Seattle, was riding the crest of the country's economic boom. Sales of construction and farm equipment were soaring.

Today, domestic demand for those same tractors, backhoes, and excavators is still strong. But Triad and other equipment dealers are bracing for a tidal wave that could sweep away their profits for the next two years—a flood of “gray-market” goods washing ashore from recession-stricken Asia. Builders in places such as Malaysia and Japan have halted projects, and now the machines they ordered—and usually have never used—are coming back into the U.S. market for sale at prices sometimes 50% off list.

The result is that customers who might have been kicking the tracks on one of Triad's Link-Belt excavators are bargaining instead on barely used equipment arriving at U.S. ports from Asia. “It's like watching a tsunami build and not being able to do anything about it,” says Triad branch manager Michael Coogan, who first noticed the uptick in gray-market products back in September.

DESPERATE DAYS. The deals are lush. Some gray-market equipment is selling for as little as 60% of what U.S. dealers pay wholesale. Excavating contractors in the Chicago area say prices are so low for equipment coming into ports in Washington and Oregon that it's easy to justify paying an additional \$2,000 in transportation costs to ship the equipment to the Midwest. No warranty? No problem. At these prices, the machines can be rebuilt once and still be cheaper than a new machine, says one purchaser who asked not to be identified for fear of spoiling relations with dealers.

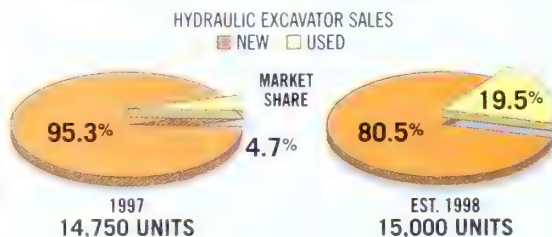
For their part, manufacturers such as Caterpillar, Deere, and even Komatsu America—which is threatened by these imports as well—say only that the gray mar-



TACOMA: Clogged docks after the Asia crisis

ket is on their “radar screen.” However, they may not escape the fallout. In February, analyst John E. McGinty of Credit Suisse First Boston downgraded Cat stock and predicted that “gray iron” will take over half of the 1998 excavator market. Such inroads could represent well over \$1 billion in sales.

GRAY MARKET'S BIGGER BITE



And the gray market isn't limited to excavators. Tractors and backhoe loaders are beginning to appear on the docks, too. In a survey by the Associated Equipment Distributors, a trade group, 40% of the nation's heavy-equipment dealers reported that they are competing head-to-head with gray-market brokers—who include auction houses, entrepreneurs, and used equipment

dealers. “It isn't staying confined to the West Coast,” says Frank Manfredi, an industry consultant in Mundelein, Ill. At the Port of Baltimore, inbound shipments of used excavators have jumped from almost nothing to 148 tons between September and January.

Meanwhile, dealers are scrambling to craft a strategy to fight back. They're appealing to manufacturers to lower their prices, give dealers a chance to defend their market share. And they're launching advertising campaigns extolling the loyalty between customers and the dealerships they've dealt with for years.

CRUNCH TIME. On Mar. 25, members of the AED met in Virginia to refine strategies for fighting back. “My first inclination was to say ‘Let's buy the equipment ourselves and to hell with the manufacturers,’” says Anthony Obadal, the AED's general counsel. However, he says that concerns about getting stuck with equipment that violated federal safety and emissions standards—typical of machinery built in Asia for overseas markets—prompted the dealers to abandon that option. Instead, the AED decided to urge Congress to support strict

enforcement of such federal standards by imposing hefty new fines against violators.

Can the dealers move fast enough to turn the tide? March is the beginning of the six-month selling season. During this period, about 75% of annual equipment purchases will be made. Meanwhile, some \$2 billion in early-moving machines could be arriving from across the Pacific, according to gray-market broker Michael Zinman of New York. “Coming right now, \$2 billion on the market could collapse it,” he says. In the end, the only real option for dealers and manufacturers may be to wait—at least until the supply from Asia is exhausted or Asia needs the equipment again.

By De'Ann Weimer in Chicago

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MEDIA

BOLDLY GOING WHERE OTHERS ARE BAILING OUT

Why does Bertelsmann think it can profit with Random House?

What's behind the massive foray into the American book publishing business by German media conglomerate Bertelsmann? Spend a moment at the company's U.S. headquarters in the heart of Times Square and you soon find out. Chief Executive-elect Thomas Middelhoff discusses big plans for book publishing while gesturing out a 22nd-floor window—to the headquarters of Viacom Inc., the rival media conglomerate. "We have a much stronger relationship to the book business now than Viacom, Walt Disney, Time Warner, or News Corp.," Middelhoff says in German-accented English.

That was Middelhoff's intent in November when he approached media mogul S. I. Newhouse with an offer for Random House, the country's biggest book publisher. The Mar. 23 deal, estimated at \$1.4 billion, gives the Munich-based parent of Bantam Doubleday Dell Publishing Group Inc. 15% of the U.S. market. When it closes, nearly 40% of Bertelsmann's \$16 billion in revenues will come from books.

But why is the world's third-largest media company adding book publishing properties just as rival media giants are looking for a way out of the ailing industry? Sales of consumer books slid 3.4%, to \$5.4 billion, in 1997, according to the Association of American Publishers, as fees to superstar authors spiraled, along with returns of unsold

SQUEEZE "It's becoming harder and harder to make money," says Penguin President Phyllis Grann

books. And profits are slim. Viacom's Simon & Schuster generated \$200 million in profits in 1997—but the unit's margins were a third of those for Viacom's cable and broadcasting operations. Now, Viacom is selling at least part of Simon & Schuster. "It's becoming harder and harder to make money," laments Phyllis Grann, president of Penguin Putnam Inc.—a company that was created

when Seagram Co. sold Putnam Berkeley Group to Pearson PLC in 1996.

Things weren't much better at Random House, a unit of Newhouse's Advance Publications Inc. Random House is one of the most revered publishers in the world, with a rich history in literature and an ability to cater to the mass market with best-sellers such as *Primary Colors* and *Midnight in the Garden of Good and Evil*. Last year, revenues were estimated at \$1.2 billion and profits were in the high single digits. "This is a gem they sold," says CEO Alberto Vitale, who will be replaced by Bertelsmann executive Peter Olson.

NEWCOMERS. But two decades after Newhouse paid \$60 million for Random House, the unit's profits did not rival those of Advance's magazines and newspapers. "With a third generation coming up," says the 70-year-old Newhouse, "we had to make strategic decisions."

So why do books make sense for Bertelsmann? It owns Arista Records Inc., European broadcasters, and a chunk of America Online Inc., but its business centers on books. Begun in Gutersloh, Germany in 1835 as a Christian bookbindery, Bertelsmann runs book club with 35 million members in Europe and North America. It will soon extend its vertical integration when it begins selling online, positioning itself to become the world's biggest book merchant. "Book publishing is not a stepchild here," Olson says. "It is our focal point."

Bertelsmann's book business is just as profitable as sister units, Olson says. Insiders say Bantam Doubleday Dell has profit margins in the low-teens—high for book publishers—with two key drivers: authors John Grisham and Danielle Steele. Bertelsmann also runs a more centralized operation than other companies with multiple imprints. "The force executives to be team players as opposed to looking out for their own

turf," says Robert Gottlieb, an agent whose clients include Tom Clancy.

Book publishing could become even easier for Bertelsmann if it expands

into U.S. broadcasting, letting it cross market. It has long considered buying a film studio and may challenge a federal rule barring foreign ownership of TV stations. "We're not foreign," Middelhoff says. "We're international. I'm an American with a German passport." Book publishing, anyway, Bertelsmann is now as American as Disney.

By I. Jeanne Dugan in New York



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WALL STREET

A GOLDEN MOMENT FOR GOLDMAN SACHS?

Should it go public, the partners would divvy up billions

Yet again, the Goldman Sachs-is-going-public rumor is sweeping Wall Street. Never mind that Goldman Sachs & Co. is thriving as a privately owned partnership, posting eye-popping pretax profits of \$1 billion on revenues of \$2.5 billion in its fiscal first quarter.

A Goldman Sachs spokesman insists that the firm "has no plans to go public." Last December, Goldman Chief Executive Jon S. Corzine told *BUSINESS WEEK* that going public wasn't even on the agenda for 1998. Yet a strategy committee headed by Goldman President Henry M. Paulson Jr. is evaluating the firm's structure, possibly to make recommendations at the June 12 annual meeting. Some partners acknowledge that with the stock market at record highs, this could be a good time to float a public offering. Says one Goldman source: "There is a debate going on in the firm about whether to go public."

SPREAD THE WEALTH? If Goldman decides to take that step, it would be a massive IPO. It's a "huge payday," says one investment banker. "The value unleashed is phenomenal." One good way to estimate the size of the deal is to use book value. Competitors Morgan Stanley Dean Witter & Co. and Merrill Lynch & Co. trade at 3.5 times book value. Thus Goldman, which has \$6.3 billion in equity capital, the equivalent of book value, might be worth about \$22 billion.

Such a deal would represent one of the biggest bonanzas any Wall Street firm has ever seen. More amazing still is that most of these riches would go to just 190 Goldman general partners. Say Goldman Sachs sold for \$22 billion. The firm would first have to repay \$2.2 billion to general partners and about \$3.8 billion to various limited partners and a grab bag of firms and individuals with capital in the firm: Japan's Sumitomo Bank Ltd., Hawaii's Bishops Estate, and insurance companies, as well as retired general partners and nonpartner employees. But after paying back that \$6 billion, Goldman partners would have \$16 billion left to divide.

The division would be based on partners' ownership percentages, which range from about 0.25% to 1%. That would mean a cool \$160 million for top brass such as Corzine. Junior partners would have to settle for something like \$40 million.

However, that's only theoretical—and pretax. It does not take into account how the company would approach its post-IPO future. The 190 Goldman partners would want to spread the wealth to keep their fellow employees at the firm.

Goldman's general partners hold all the cards: Though they own only 36% of the firm's capital, they have 100% of the voting power. But they will probably compensate the firm's best nonpartners, from about 200 new non-equity-owning managing directors to senior vice-presidents. This could be done with stock or stock options. For example, when Robertson Stephens & Co. was sold to BankAmerica Corp. last June, its 60-odd partners set aside \$70 million of

their \$433 million take for employee who were just below partner level to retain them.

GENERATION GAP. Goldman partner may also want to placate the firm's limited partners, especially retired general partners. Dividing up the pie is sure to be painful. Says one banker: "The new guys always think the old guys don't deserve anything. The old guys say 'You just want to get rich quick, we built this firm.'"

Goldman would probably do an IPO of about 15% of the firm, raising roughly \$3.3 billion. The remaining 85% would stay in the hands of the general partners and others. Their partnership interests would be converted into stock.

The pain should be a lot less severe than it would have been in early 1990 when the firm last considered going public. That's because Goldman demographics have changed dramatically. At the time, there were many new partners who owned very narrow slices of equity and who were vehemently opposed to going public. After three very good years, these partners have fattened their stakes. Just one more reason why the perennial Goldman-is-going-public rumor is coming around again.

By Leah Nathans Spiro in New York



CORZINE: An IPO isn't on the agenda

Big Deal

If Goldman Sachs went public, how much would it sell for? Other brokerage firms have tended to sell for between three and five times their book value. Using a multiple of 3.5, Goldman, with a book value of \$6.3 billion, might bring \$22 billion.

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ROBERTSON STEPHENS	6/97	.54	5
SALOMON BROS.	9/97	9.00	2
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EDITED BY KELLEY HOLLAND

THE BEETLE AND THE CROWN JEWEL

THE GERMANS ARE TURNING out to be Rolls-Royce enthusiasts after all. Ending weeks of rumors, Volkswagen CEO Ferdinand Piëch said on Mar. 25 that he has bid on the storied British luxury carmaker owned by Vickers, the British industrial group. The move could enable VW to join the other big German auto makers in the luxury market. BMW confirms that it also still plans to bid on Rolls, but Daimler-Benz says it isn't interested. At least two British bids, including one by a management group, also are being planned. Piëch wouldn't say how much he offered, but analysts expect Rolls to fetch \$500 million or

so. The bidding will likely continue into April.

WATCH TV—AND PAY THE BILLS

COUCH POTATOES, PREPARE to balance your checkbooks. Cable giant TCI has signed a preliminary deal with BankAmerica and Intuit to provide financial services to TCI subscribers through a digital set-top box that will also offer hundreds of TV channels and Internet access. The companies are giving TCI a large up-front payment, which TCI will use to reduce the \$300 cost for each of the 6.5 million or more boxes it plans to order by 2000. Other financing deals are in the works, and cable sources say an agreement with AT&T for Internet phone service is possible.

HEADLINER: KIM EDWARDS

END OF A REIGN AT IOMEGA

HIS SPIN AT THE WHEEL IS over. On Mar. 25, Kim Edwards abruptly resigned as CEO of Iomega, maker of the popular Zip disk drive. During his four years, Edwards turned Iomega, whose products offer high-capacity backup storage for PCs, into a high-tech highflier. Driven by heavy spending on catchy ads, sales skyrocketed to \$1.7 billion from \$141 million, and Iomega's stock became a Wall Street darling.

But the company has been losing its luster. On Mar. 16, Iomega told Wall Street it would likely post a loss of \$10 million to \$25 million in the first quarter,

thanks to tough competition, high marketing costs, and a slump in the market for peripherals.

Edwards' marketing budget was already a sore point with investors. In January, when Iomega reported lower fourth-quarter earnings, Edwards

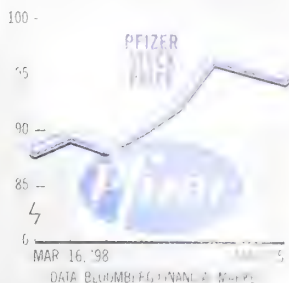
told analysts he would more than triple the budget to \$100 million. Iomega's shares fell 31%. On Mar. 25, the shares closed at 7. Edwards couldn't be reached for comment. Taking over for now is director James Sierk, most recently a senior vice-president at AlliedSignal.

By Ira Sager

CLOSING BELL

POTENCY PLAY

Pfizer is getting quite a lift from Viagra. On Mar. 23, Pfizer stock rose 4.5% to close at 96%, after the ABC News program 20/20 did a segment on the company's promising new impotence treatment. Viagra, which may win marketing approval from the Food & Drug Administration any day now, is expected to be a blockbuster, with possible annual sales of \$3 billion by 2002. More good news on Mar. 24: Pfizer announced that its deal to promote G. D. Searle's upcoming arthritis drug was expanded to include all areas of the globe except Japan. But that wasn't enough to keep its stock aloft, and it closed Mar. 25 at 94%.



THE FTC EYEBALLS LASER SURGERY

LASER SURGERY TO CORRECT nearsightedness has the Federal Trade Commission seeing red. On Mar. 24, in an administrative complaint, the FTC charged that Summit Technology and VISX used a price-fixing scheme to overcharge consumers by \$30 million in 1997. The companies are the only ones approved by the FDA to provide the lasers used in the procedure. But instead of competing, the FTC says, they formed a partnership to share patents and doctors' licensing fees. As a result, the FTC says they have been reaping monopoly profits. Both companies deny the allegations. They are also suing each other over strains in the partnership, which the FTC wants to dissolve.

RATINGS SERVICES RUSH THE NET

THERE'S A RACE TO become the ACNielsen

of the Net—and it includes Nielsen itself. On Mar. 30, NetRatings, a startup backed by Hitachi, is entering a fragmented market and launching a service to rate the popularity of Web sites. Nielsen plans to join the fray this summer. "As the Internet moves to TV, it becomes much more important to us," says Manish Bhatia, Nielsen's vice-president of interactive services. At stake: sales of ratings to help advertisers gauge audience size as they spend more on Net ads, which could hit \$8 billion by 2002.

WILL TELETUBBIES TRAVEL?

MEET TINKY WINKY, Dipsy, Laa-Laa, and Po (left). They're Teletubbies, and they'll make their U.S. TV debut Apr. 6 on PBS. The characters have ignited

a Beanie Babies-style mania in Britain. If they catch on stateside, it could mean big bucks for Hasbro, Scholastic, and Warner Home Video, which will peddle Teletubbies products. Handleman, a co-distributor, is rumored to have a 47% stake in the U.S. licensor of Teletubbies, and some investors are betting on the craze via that stock. But it's unclear how American parents will react to Teletubbies, which are aimed at kids as young as 12 months.

ET CETERA...

- Smaller is beautiful: Wal-Mart plans to open three small stores.
- CVS will issue 18.9 million shares as part of its plan to purchase Arbor Drugs.
- Delta Air Lines hired New Chief Financial Officer Warren Jenson to be its own CFO.
- Korea is planning an international bond sale of up to \$4 billion.





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cover annual mammograms for all women over 40. We know what it costs, but by treating breast cancer in its earliest stages, we also know what it can save. ■ The best care can even halt the progression of chronic disease. Our congestive heart failure program provides a cardiac nurse to educate at-risk members on the importance of taking prescribed medications, and to help them make lifestyle adjustments. The result has been a significant decline in hospitalization rates and an overall improvement in patient well-being. ■ Not coincidentally, our model of prevention, early detection and chronic disease management promotes better health, with the added value of lowering health care costs. Which in turn enables companies such as ours to provide more people than ever the best choices modern medicine can offer. And do so without offering the one choice no one should ever again have to make: Their money? Or their health?



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TAX REFORM: THE GOP FUMBLES ITS DREAM ISSUE

was supposed to be the Republicans' best photo op of the election year: On Apr. 15, beaming lawmakers would stand around President Clinton in the Rose Garden to watch him sign a GOP-backed bill that clamps down on abuses by a runaway Internal Revenue Service. So much for that Kodak moment. The GOP's popular drive to overhaul the IRS has run afoul of intraparty squabbling. Republicans aren't just going to miss their symbolic tax-reform headline—they're in danger of blowing the issue altogether. "Every day we wait increases the likelihood that we won't pass anything and taxpayers will lose," grumbles Sen. Bob Kerrey (D-Nebr.), co-chair of the panel that first called for IRS reform. The hang-up is in the Senate. Finance Committee Chairman William V. Roth Jr. (R-Me.) was supposed to deliver a bill by March 30. But he doesn't want the Senate to wait until he stages another round of hearings in April. The new sessions, likely to focus on IRS tactics in criminal cases, aren't expected to boost the overhaul measure, which passed the House by 426-4. But Roth, who has lost at House bids to claim credit for the issue, wants to remind Beltway players that it was his hearings on IRS excesses last year that blew away White House opposition to reform.

DRAGGING UP A TAB. During the delay, senators are piling on protections that are driving up the bill's cost. Senator Christopher S. Bond (R-Mo.) wants to cut into the \$7.5 billion the IRS collects in penalties each year. He's pushing to eliminate "substantial underpayment" and "failure to pay" levies. His costliest idea would halt IRS efforts to collect taxes from spouses who innocently sign a fraudulent joint return. The Senate bill's 10-year tab comes to \$20 billion—more than triple the House measure's cost. Under budget rules, lawmakers must offset lost revenue with cuts or tax hikes.

Some conservative Republicans want to make sure taxes don't go up. Taxpayers shouldn't have to pay for protection from the IRS, these lawmakers say. They want the costs to come out of already approved spending, not tax hikes or even obscure loophole-closers. Roth says he has found ways to offset his bill's cost, but won't disclose them.

Roth's personal touches on the bill also will slow things down. His proposals, unveiled on Mar. 24, would undo a



ROTH: Wants more hearings

House deal that won Clinton's grudging acceptance. Roth would boot the Treasury Secretary off a new IRS governing board, while boosting the panel's powers over tax-law enforcement. Other senators want to make the IRS even more independent: They would turn the part-time board into a permanent bureaucracy that would replace the Treasury as the agency's overseer. That's sure to draw a veto recommendation from Treasury Secretary Robert E. Rubin.

The Senate's target now is to vote on an IRS bill in May. But that's the height of the budget season. Reformers fear their bill will turn into a vehicle for GOP tax-cutters, who could add on amendments that would trap it in an internal fight over how best to use a projected surplus.

All the skirmishing adds up to election-year trouble for the antitax party. Republicans want to replace the income tax but can't agree on a plan. The GOP's other big tax issue—repealing the tax code by 2001, even if there's no replacement ready—has laid an egg in polls.

That leaves only one tax idea Republicans can agree on: They all hate the tax collector. But if the party lets IRS restructuring founder, GOP candidates could go home this fall with nothing to say when taxpayers ask: "What have you done for us lately?"

By Mike McNamee

CAPITAL WRAPUP

CAMPAIGN CLEANUP?

The Federal Election Commission, seen as a toothless tiger by campaign-finance reformers, wants to put some teeth back into federal campaign disclosure laws. It's asking Congress for power to streamline disclosure rules, require electronic filings, and get more frequent fund-raising reports. With a major campaign-finance overhaul dead this year, the FEC's bipartisan recommendations represent a last reform. The commission also has a political motive for acting: A

House panel has scheduled a Mar. 31 hearing on the FEC's failure to pursue evidence of illegal foreign donations.

PLAYING MUSICAL CHAIRS

► House Committee chairs don't have to step down until 2000 under GOP-imposed term limits, but the jockeying already has begun to replace Ways & Means chief Bill Archer of Texas. A top candidate is California's William M. Thomas, chair of the tax-writing panel's health subcommittee. He has been a big booster of tax-deferred medical savings accounts.

BIG BROTHER AL

► Al Gore's call to protect kids from cyberspace "red-light districts" is drawing gripes about Big Brother from Internet denizens. On Mar. 23, the Vice-President urged Congress to require Net-connected schools and libraries to develop plans to filter out porn. Complains Net consultant and ex-Clinton cyberspace guru Jock Gill: "Please get the government out of my relationships with my children." Gore's response: Schools are free to choose their own form of controls.



BEIJING'S GREAT HALL

Zhu announced his plans at the National People's Congress in late March

clearly, China's new leaders are poised to dismantle much of what is left of central planning.

In some areas, the government intends to step up programs already under way. Beijing plans to increase spending on railway by 25%, to \$5.4 billion, and hike its already massive investment in new phone lines. Elsewhere, Zhu is speeding up reforms that were to be phased in over many years. Take the drive to end subsidized housing by yearend. Beijing wants more Chinese to own their homes, partly because new homeowners invest an average of \$7,000 to spruce them up. But

most Chinese pay only about \$5 a month for employer-owned flats, so few are buying. The plan, says Wu, is to hike rents as much as fourfold. Workers then will be offered raises that can only be used toward buying their flats. Also, Beijing will increase the supply of mortgages and low-cost housing.

Sweeping bureaucratic reforms also should stimulate growth. Currently, companies owned by bodies such as the Posts & Telecommunications Ministry (MPT) dominate industries they regulate. As a result, MPT-controlled China Telecom Ltd. has few competitors. But the MPT will be folded into another ministry, reducing its power, and China Telecom will sell noncore businesses, such as satellite services. "China Telecom is in position of state monopoly," says Wu. "We are going to break that monopoly."

In another key rupture with tradition, Wu says Beijing will "actively promote the nonstate sector"—meaning private enterprise—and service industries. These sectors now are seen as critical sources of jobs. Foreign investment also is likely to be liberalized. Beijing's decision to allow Eastman Kodak Co. to take over ailing Chinese film manufacturers is seen as a breakthrough.

Some still think Zhu isn't going far enough. Controversial plans to create giant state-owned business groups are going ahead. And there are doubts the Communist Party is really ready to cede so much control. But if Zhu's team succeeds, China will have made a huge leap toward a true market economy.

By Dexter Roberts, with Joy Barnathan and Robert J. Dowling, Beijing

CHINA

NOW, IT'S REFORM OR BUST

The details of Beijing's bold plan are starting to emerge

After months of political intrigue and closed-door policy debates, Beijing's new technocrats face a daunting task: figuring out how to implement the ambitious economic agenda unveiled by new Premier Zhu Rongji in late March at the National People's Congress. The objective is to keep China's economy growing at an 8% clip at a time when consumer spending is drying up and the rest of Asia is in crisis. What's more, in just three years, Zhu wants to overhaul China's financial system, state industries, and bureaucracy—goals that have frustrated reformers for decades. It's "no easy job," concedes Vice-Premier Wu Bangguo in an interview with *BUSINESS WEEK* (page 55).

Wu provided an early look at many of the details of China's bold new plan. The main thrust is a big boost in public spending—at least \$30 billion in new funds this year alone, says Wu, 56, who is second only to Zhu in setting economic policy. Most of this investment, to be financed largely through greater bank lending and public borrowing, will

be in housing and infrastructure. But the plan also calls for opening the economy to new competitors by shrinking Beijing's role in key industries and boosting the private sector.

BAD LOANS. The pace set by Zhu and his deputies is breathtaking. By yearend, they aim to end China's system of subsidized housing. More than 4 million civil servants will lose their jobs when one-quarter of China's ministries and commissions are eliminated. Within three years, Zhu expects to restructure the nearly insolvent banking system and wipe out hundreds of billions of dollars in bad loans. Economists doubt if such a transformation can be achieved so quickly. But

Can the bureaucracy, state industries, and banks be overhauled in just three years?

A TALK WITH VICE-PREMIER WU BANGGUO

Chinese Vice-Premier Wu Bangguo, 56, typifies the new breed of technocratic leaders in Beijing. A former party boss from Shanghai, he now supervises state enterprise reform. In the Purple Light Pavilion of Beijing's Zhongnanhai compound, top leaders, Wu spoke confidently to *BUSINESS WEEK International's* Managing Editor Robert J. Dowling, Asia Regional Editor Joyce Barathan, and Beijing correspondent Dexter Roberts about China's economic problems and how the new leadership intends to tackle them.

Q: How has the Asian financial crisis affected the Chinese economy?

The crisis has not yet had a large impact on China. This is reflected by the fact that China's currency has not been devalued. But 60% of China's exports go to Asia, and 80% of foreign investment comes from Asia. And many imports, including processed oil, petrochemical products, and steel are coming in from South Asia. So this will pose a challenge to future economic growth.

Q: How will China respond?

We are going to increase domestic demand. Vice-Premier Li Lanqing said that within the coming three years we are going to invest \$750 billion. The reality may be more. For instance, this year domestic investment might be as high as 2.8 trillion renminbi, more than \$300 billion.

Q: How will you finance it all?

In the past few years, fiscal revenue has increased very rapidly. We do know that the saving rate in China is high. And we're now gradually developing the capital markets.

Q: Explain the housing reforms.

At the moment, housing is mainly provided as a form of welfare. We are going to change it into a commodity. After that is accomplished, it will be a cost to the overall national economy.

Q: What are the main problems facing China's state enterprises?

The number of state-owned enterprises is very big, but most are too small. And they are scattered about China. There also is low-level, duplicate production.

Q: Given what's happened to Korea's

big conglomerates, are you reconsidering mergers of big state companies?

A: We see that competitive countries all have very large enterprises. Technological innovation is mainly dependent on these multinational companies. One can learn from experience. The functions and administration of the government must be separated from the enterprise. The reorganization of state enterprises should be based on market considerations rather than government ones. Second, when you merge enterprises with [different lines of business], you must be very prudent. The new groups must have very competitive core businesses. Third, the enterprises must not be overly in debt.

Q: How will you resolve bad debts in the state sector?



MARKET MAKER

"Housing is mainly provided as a form of welfare," says Wu (with translator). "We are going to change it into a commodity"

A: In the past, an appropriation from the budget was considered a loan, and that went down as debt for the enterprises. We are now going to change loans into investments. Last year, more than 30 billion renminbi (\$3.7 billion) of loans were turned into investment, and this year we'll do an additional 50 billion (\$6.1 billion). We are encouraging mergers, regulating bankruptcy procedures, and downsizing the enterprise staffs to improve efficiency. Some of the enterprise debt

may be written off. Enterprises with a competitive edge can issue stocks.

Q: How serious will unemployment be, and how will you address it?

A: Altogether, there are 10 million people who need jobs. With the deepening of state enterprise reform, we estimate that 4 million people will be laid off annually. These figures are always on our minds. Our objective is to absorb these people over five years. First, we are going to ensure that the laid-off workers receive a minimum subsistence allowance that will also cover pension and medical care. The second measure is to provide job opportunities. In China, the service sector is not well developed, providing only 26% of jobs. The non-state sector can provide 16,500 job opportunities every day. We will pro-

vide laid-off workers seeking to be self-employed with favorable taxation, credit, and approval policies.

Q: How will the climate improve for foreign investors?

A: We will lose no time in studying the issue of further opening up the construction industry, accounting, legal, and financial services. But [we will move] with caution and care.

Q: Can you really finish such a huge economic program in three years?

A: I think we will definitely complete it.

For an extended version of this interview go to America Online: Keyword: BW or www.businessweek.com.

THAILAND

CAN CHUAN TURN THAILAND AROUND?

The country is taking baby steps on a risky course of reform

These are heady times for Thai Prime Minister Chuan Leekpai. His four-month-old government has won praise for pushing through reforms mandated by the International Monetary Fund's \$17 billion bailout package. Feted in the U.S. in early March, Chuan left with \$1 billion in Export-Import Bank credits, a release from a contract to buy military planes, and an endorsement from President Clinton urging investors to return to Thailand. No wonder optimism is growing. "The overall situation is much better than three or four months ago," Chuan told **BUSINESS WEEK**.

So is Thailand, the first nation to plunge into Asia's currency crisis, now the first to turn the corner? In some senses, yes. The government is, by the reckoning of the IMF, putting in place the reform measures necessary to get Thailand growing again. And the currency and stock market seem to be stabilizing. "We are no longer drifting down to disaster," says Chumpol Nalamlieng, president of industrial giant Siam Cement Co., which has \$4.1 billion in unhedged debt and lost a record \$1.3 billion last year.

But shocking numbers like those indicate just how much pain Thai compa-

nies are enduring. Chuan's government estimates that over the next three months, the economy will contract at an annual rate of 6.5%—a recession much deeper than the one predicted by the IMF. While the baht may be rising so is unemployment. The stock market is recovering, but high interest rates continue to cripple companies. While the trade surplus is building, it's largely a result of plummeting imports rather than surging exports. Even Chuan admits, "the full impact of the crisis has still to be felt."

"THE EASY PART." For all its woes, Thailand is far ahead of fellow IMF patient Indonesia and South Korea in instituting reforms. So political leaders and executives around Asia are watching how it copes as it struggles back to prosperity. What they see is that even a country saddled with cronyism can begin getting its house in order. What they are eager to find out is whether Chuan is willing to follow IMF-mandated reform with even tougher measures.

Such steps include allowing foreign investors for the first time to contro-

A Reform-Minded Premier

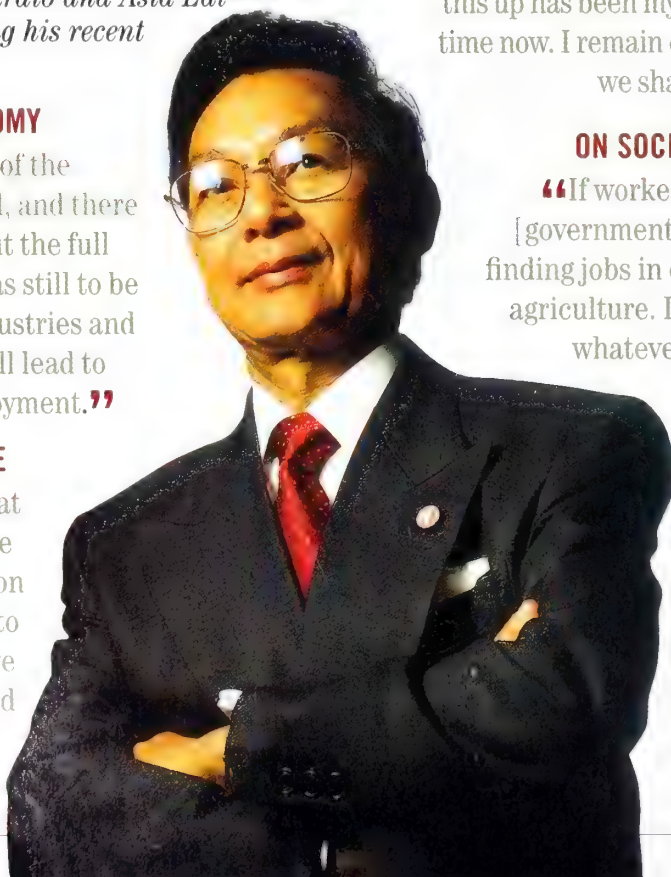
Chuan Leekpai believes pain will precede any recovery. He discussed his views with Senior News Editor Pete Engardio and Asia Editor Sheri Prasso during his recent trip to the U.S.

ON THE ECONOMY

"The volatility of the currency has lessened, and there is more stability. But the full impact of the crisis has still to be felt, especially on industries and businesses. This will lead to layoffs and unemployment."

ON FREE TRADE

"I don't believe that within ASEAN there will be a retrogression in our commitment to free trade because we are already committed to [free-trade agreements]."



ON CORRUPTION

"In several periods in our history, the government has not been honest. To clean all this up has been my objective for a very long time now. I remain confident that eventually we shall prevail."

ON SOCIAL PROBLEMS

"If workers are laid off, the [government] will assist them in finding jobs in other sectors, such as agriculture. I am confident that whatever happens, no Thai will go hungry."

ON JAPAN

"The leadership role they have displayed is less than could be expected... We can expect increased pressures from the affected countries on Japan to play a greater role."



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big pieces of the banking, financial, real estate, and manufacturing sectors. Opening up these areas would bring transparency to corrupt sectors and give the Thais needed liquidity. "What has happened so far is the easy part," explains Charnchai Charuvastir, president of the Thailand Management Assn. "The difficult part is next."

Chuan has started down the right track. He has forced the banks to recapitalize and has shut down dozens of finance companies—the go-go lenders that fueled the bubble economy with easy credit. Foreign investors are now allowed to take 100% stakes in them for up to 10 years. This is aimed at the system of banks and finance companies that funded the country's well-connected business elite. By forcing families that control the big banks to dilute their ownership, Chuan may go a long way toward solving some of Thailand's chronic problems. Moreover, with a new constitution passed last year and tighter regulation, the economy has become less prone to abuse.

NO NEW CREDIT. Those hopeful steps are leading some investors to start returning to the beleaguered manufacturing sector. In March, George Soros chipped \$3.5 million into a \$650 million package for Nakornthai Strip Mill. Such deals, however, are a rarity.

Luring back foreign investment will be essential as the banks tackle the task of restoring their balance sheets. Burned by loans gone bad, banks and finance companies are refusing to extend new credit to companies. Instead, they are parking funds with the central bank, buying government bonds at interest rates of 21%. "It's low risk and very liquid," says Sripop Sarasas, managing director of Phatra Thanakit, one of the major finance companies still active despite losing \$150 million last year. "There's no such loan like that." Phatra will not resume lending anytime soon.

This kind of conservatism is painful for businesses that need capital, and a new government agency could force the banks to tighten even more. The Financial Sector Restructuring Authority (FRA), modeled on the Resolu-

tion Trust Corp. of the U.S., is in charge of selling off property-backed loans as well as cars, paintings, and even office furniture of the 56 closed finance companies. Vicharat Vichit-Vadakan, the head of the FRA, vows to let market forces determine prices. "We want to address the issue as quickly as possible," he says.

The banks, which lent generously to real estate projects launched by the finance companies, are bracing for big write-downs in their property portfolios once the FRA starts selling off assets. The banks now carry property on their books at inflated, pre-bust values.

Another worry is that the government will never re-

cover some \$11 billion in state loans pumped into the finance companies in futile bid to keep them afloat. That means the government may starved for cash at a time when it cannot raise taxes for fear of crushing the economy. Simply writing off the loans would be politically risky, since it signals that fat cats were bailed out at taxpayers' expense. The only way out may be to print more money. "There will continue to be the temptation to inflate their way out of the problem," says Sriyan Pietersz, at SocGen-Crosby R

search. Already, Thailand's wholesale inflation rate is up to 20%, he says, but markups haven't yet been passed on to consumers.

That means the risk premium on the baht is unlikely to come down soon. And killing interest rates will stay high since a weak baht would quickly scare off the foreigners now pouring into the stock market. The Bangkok exchange's surge since January is nothing but a "bear market trap," asserts Russell J. Kopp, head of research at Dresdner Kleinwort Benson Securities' Thai office.

HANDS-ON BOARDS? Yet the Thais willingness to acknowledge their role in the crisis could help them as they dig their way out. Changes such as making directors more responsible for overseeing management could revolutionize the way companies are governed, says Charnchai of the Thailand Management Assn. Other moves he would like to see: tougher bankruptcy laws, foreigners allowed to own property and operate businesses without restriction, and privatization of transportation and key industries.

The most pessimistic observers are willing to concede that the Thai government has made some impressive moves. But even with a government tuned to fixing Thailand's problems, recovering from years of mistakes will take a long time. The Thais deserve praise for starting down a difficult path. Now, the world is watching to see if they can finish the journey.

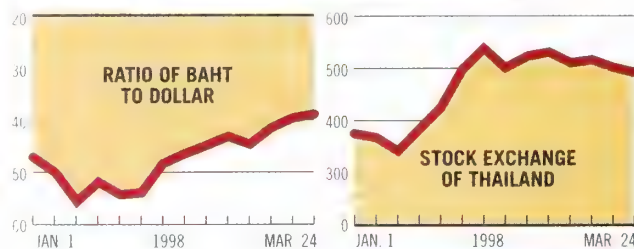
By Bruce Einhorn
in Bangkok

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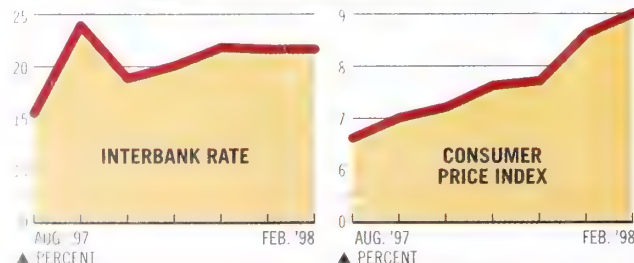
Work hasn't halted on Bangkok's light-rail transit system



GOOD NEWS: THE BAHT IS STRENGTHENING AS THE STOCK MARKET IS RECOVERING



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EDITED BY JOHN TEMPLEMAN

YELTSIN'S MARCH MASSACRE MAY CLEAR THE WAY FOR REFORM

President Boris N. Yeltsin stormed back from a weeklong illness in signature fashion. Eager to show he was still in control, on Mar. 23 he fired the entire Russian government. One clear aim was to slap down former Prime Minister Viktor S. Chernomyrdin, who was acting as if he already had the 2000 presidential election in the bag. Chernomyrdin, wags say, was beginning to make Yeltsin look like a political corpse even though his presidency has two years to go.

But the March massacre goes far beyond personality conflicts. Yeltsin is attempting to ensure that Russia's transformation into a capitalist democracy doesn't derail. To do that he needs to make reform much more palatable to voters and to stomp out Russia's brand of crony capitalism. Yeltsin's bold move was to remove government ministers who had direct ties to Russia's oligarchical banking and energy barons. He is replacing them with a generation of young leaders who favor reform and a more competitive market. Surprisingly, some moguls agree it's the way to go.

Analysts expect Yeltsin's new team will try to implement policies that Russia needs to establish a more fair and orderly economy. They range from creating a new tax code and a workable customs system to breaking up monopolies and building a social safety net. "You'll end up with a Prime Minister less inclined by habit and personality to favor the status quo and less tied to the oligarchies," says Charles Blitzer, a former World Bank economist now at Donaldson, Lufkin & Jenrette Inc.

By firing Chernomyrdin and First Deputy Prime Minister Anatoly B. Chubais, Yeltsin struck a blow at the fat cats. As its former chairman, Chernomyrdin is closely linked to Gazprom, Russia's gas monopoly. And Chubais devised the privatization program that allowed a small group of bankers to get rich by snapping up big state companies, such as Norilsk Nickel, at giveaway prices in 1995 and 1996.

Yeltsin certainly doesn't want to feature in history books as the man who crushed communism only to replace it with an equally unfair oligarchy. But short-term electoral politics are still a big consideration. Between them, the government and the oligarchs control Russia's three national TV networks and most of the major newspapers. Over the past several months, they have given extensive and favorable coverage to

Chernomyrdin as presidential front-runner. Indeed, some of the coverage was so biased that Yeltsin needed to counter the growing public perception that the oligarchy had already sewn up the election two years ahead of time.

The President made his move at a time when business leaders were fighting among themselves. Since last summer they have battled viciously over the final juicy assets that the government has been selling off. Their growing divisions weakened their political clout and gave Yeltsin an excuse to oust their close friends in government.

Ironically, as elections approach, the oligarchs now know that it is in their best interest to support Yeltsin in his push for a Western-style market system. Most state assets have already been divvied up. That leaves less for the moguls to fight over. It also means that they must make hanging on to what they've got their main priority. So, instead of fighting Yeltsin, they need to help his government deal with Russia's pressing social problems. The government, for instance, has to ensure that wages and pensions are paid in full and on time. As long as that can't be guaranteed, the average Russian will remain disenchanted with reforms and tempted to back protest candidates such as the Communist Gennady Zyuganov or ex-General Alexander Lebed.

BURY THE HATCHET. To avoid such a damaging outcome, argues Boris A. Berezovsky, the most politically savvy of the moguls, all those who favor reform must bury the hatchet and



The President kicked the fat cats' pals out of the government

work together. In fact, he claims credit for persuading Yeltsin to dump Chernomyrdin as unelectable. Back in 1996, Berezovsky and his fellow oligarchs bankrolled Yeltsin in a desperate battle to beat Zyuganov in the presidential election. This time, both they and Yeltsin want to be better prepared for the Russian Duma elections in 1999, as well as for the presidency the following year.

Berezovsky and other moguls might have to step out of the political limelight. Yeltsin's appointment of Sergei Kirienko—a technocrat without close links to any big group—as acting prime minister is a signal that from now on they should stop meddling in the day-to-day management of the country. Russia's corporate chieftains may hate the idea. But that's the only way they will get the pro-reform president they ultimately want.

By Patricia Kranz in Moscow



Experience stage fright.

Someday I plan to: Start a business with my son. Play golf where it was invented.
Dust off my old records. Audition for a part in a play.

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THEME-PARK SHOOTOUT

A host of new competitors has Disney building like crazy

The sign out front says it's "The Happiest Place on Earth." These days, Disneyland, Walt Disney Co.'s Anaheim (Calif.) flagship, is

also one of the most construction-happy places on earth. Workers in bulldozers crisscross the 100 acres that used to be a parking lot. Outside, streets are being widened, snarling traffic in all directions. Signs tell passersby that a new Disneyland Resort is in the making.

But there's a lot more than that going on. From Anaheim to Central Florida, Disney is expanding its theme-park kingdom with gusto. Faced with stiff competition from a host of rivals that has trimmed its once juicy margins, Disney plans to spend more than \$4 billion by 2001 to add two new theme parks, a cruise line, and three regional entertainment chains. On Apr. 22, the Burbank (Calif.) company will open its first new theme park in nine years, the \$750 million Animal Kingdom near Orlando. And in May, it will unveil an update of Tomorrowland, an original Disneyland attraction.

UPPING THE ANTE. The burst of spending reflects Disney Chairman and Chief Executive Michael D. Eisner's philosophy that, despite the hoopla about cable TV and handwringing about couch-potato lifestyles, people still hunger to go out for entertainment. "I've never believed what Faith Popcorn said—that people would be 'cocooning' in their homes," says Eisner. "People get sick of sitting around their homes. They need to get out and find new things."

Maybe so. But Disney's four U.S. theme parks are facing their most in-

tense period of competition ever. From the \$2.7 billion Islands of Adventure being built by Universal Studios about 20 minutes down Interstate 4 from Walt

Disney World to new attractions such as the Wild Arctic helicopter simulation at nearby Sea World to the \$35 million in new rides planned for Knott's Berry Farm in Anaheim, everyone is upping the ante.

Those projects all take aim at Disney's most consistent cash cow. Year after year, Disney's parks provide the parent company with huge cash flow and hefty profit margins. Last year, the parks raked in \$1.1 billion in operating earnings and a profit margin of 22.7%,

compared with 16.8% for Disney's movie studios and 19.8% for broadcasting.

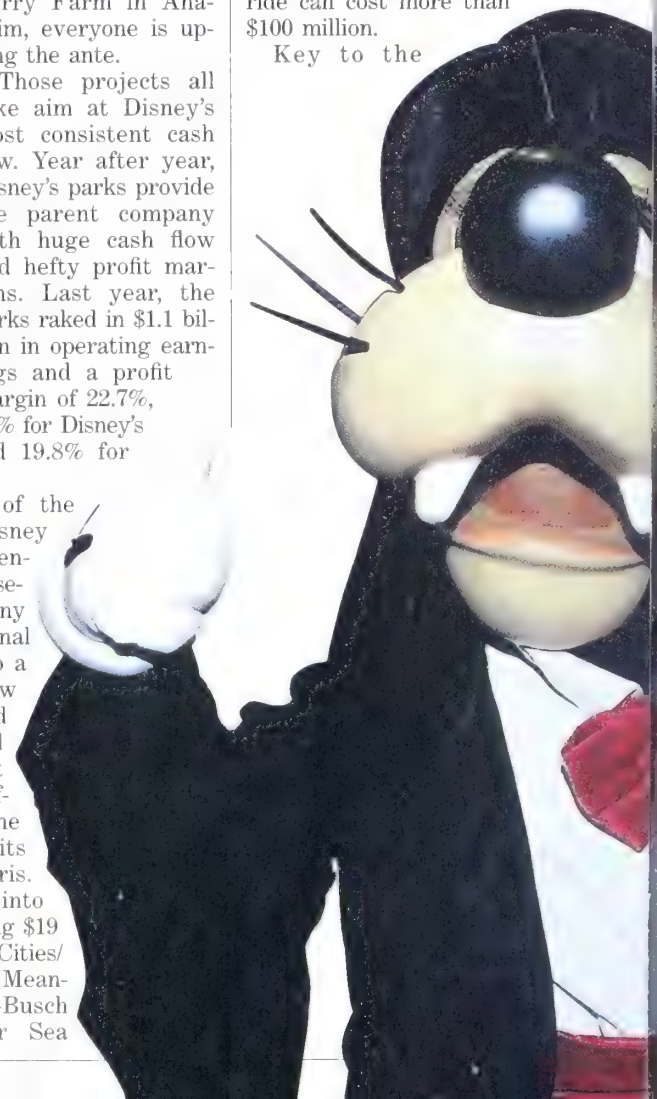
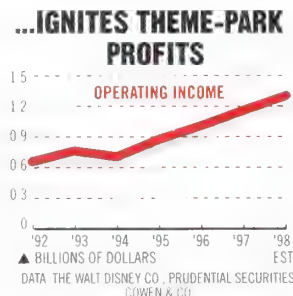
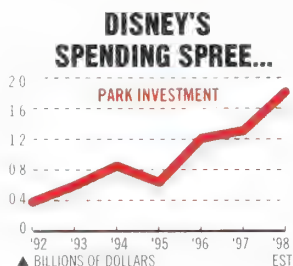
But for much of the past decade, Disney management's attention was focused elsewhere. The company dabbled in regional parks, running into a political buzzsaw with its doomed plan for a historical park in Virginia. It built overseas, suffering through the slow opening of its park outside Paris. And it branched into broadcasting, paying \$19 billion for Capital Cities/ABC Inc. in 1995. Meanwhile, Anheuser-Busch Cos. bought four Sea

World parks and began pumping in millions of dollars. Universal Studios opened a Florida park in 1990. Even Las Vegas made a play for family vacationers.

The combination of fresh vacation alternatives and a weak economy sent Disney's park attendance skidding in the early 1990s. By 1994, it had fallen 12% from five years earlier, to 39.2 million visitors annually, according to the newsletter *Amusement Business*. Although theme-park profit margins still beat those of Disney's other units, they've drooped from their far higher 30% of the late 1980s.

Disney has responded with a torrent of cash. The expansions at Universal and elsewhere "made them understand that they're not the only guys on the block," says Abraham Pizam, director of the Dick Pope Institute of Tourism Studies at the University of Central Florida. "It made them understand that they had to concentrate on quality and add, add, add." Not to mention spend, spend, spend. Today, building one new ride can cost more than \$100 million.

Key to the



gy has been expanding opera-
at the Central Florida and Ana-
strongholds. Florida is the most
tant, with three theme parks and
y 18,000 hotel rooms. But that's
where Disney faces its stiffest
etition.

ext year, a \$2.7 billion expansion of
rsal Studios Florida will open. The
cludes a second theme park, Is-
of Adventure, with Universal's
mark thrill rides, such as Dueling
ons roller coasters; a 750-room ho-
an entertainment-and-dining dis-
Citywalk, that will open later this
Universal has a sure hit in a di-
island modeled after its *Jurassic*
movie and is going after Disney's
er fans with rides based on Dr.
characters.

beat back its rival, Disney will
n in next month with Animal
dom, which features
than 1,000 types of
ls, an African safari,
rides based on such
y properties as *The*
King. The new at-
ons include Dino-
USA, featuring a
ride called Count-
to Extinction. Uni-

versal sees that as a preemptive strike
on its dinosaur attraction. "What do
dinosaurs have to do with a wild ani-
mal park, anyway?" says Cathy
Nichols, CEO of Universal Recreation
Group. Eisner deflects the charge.
"We've been working on a dinosaur
movie well before they began *Jurassic*
Park," he says, referring to an ani-
mated project.

Will it be enough? The payoff from
Disney's spending so far, analysts and
competitors agree, is that the company
has reinforced its position as the top
brand name in the business. Attendance
at its U.S. parks grew 12% last year, to
a record 53.4 million visitors, while Uni-
versal rose 4%, to 14.3 million. And
with the additional hotel rooms and
restaurants Disney is
building, it hopes to ex-
tend the average park

stay and grab even more guest dollars.

Nowhere is that clearer than in Ana-
heim, where Disney is using its clout
with city officials to build a mini-Disney
World. With Disney guaranteeing some
of the money, Anaheim is spending \$546
million to help the entertainment giant
build a resort blocked off from the col-
lection of dives and cheapo motels that
ring Disneyland. Disney is building a
750-room hotel, called Grand Californian,
to give it 2,350 rooms in Anaheim.

DRY-DOCKED. Disney has suffered some
setbacks. An effort to update Epcot
Center in Orlando ran into costly soft-
ware problems on a ride featuring cars
that race at speeds up to 65 mph. That
project is at least a year behind sched-
ule. Also, some industry skeptics ques-

tion Disney's efforts to
transfer its brand to
smaller regional entertain-
ment centers, such as its
new DisneyQuest virtual-
reality and entertainment
arcades and Club Disney
play centers for younger
children.

Disney's most public
embarrassment has been
the four-month delay in
the launch of its cruise
business because of con-
struction problems. Still,
when they finally set sail,
the two ships should help
Disney fill its parks. They
will dock at Port Canaver-
al, about 90 minutes from
Walt Disney World. To
meet its targets, Disney
needs 70% of the ships'
passengers to buy a week-
long package that com-
bines a cruise and a park

stay, says a former Disney exec. "The
whole strategic value was to get them
to the park—that's where Disney makes
a lot of money on them," he says.

And that, after all, is the real Dis-
ney magic. Recently, Philadelphia ad
exec Alex Breder was marching and
spending her way through Walt Disney
World with children Maggie, 10, and Ian,
8, in tow. Midway through a five-day
vacation, Breder figured she had spent
upwards of \$2,000 for her room at Dis-
ney's All-Star Resort, meals, park pass-
es, and trinkets for the kids. "If you're
going to spend all that money to get
here and stay, you may as well eat and
treat yourself well," says Breder.

No doubt the cash registers can be
heard ringing all the way back in Bur-
bank. But Disney can't afford to be
smug—after all, the Breder family also
planned to spend a day at Sea World.

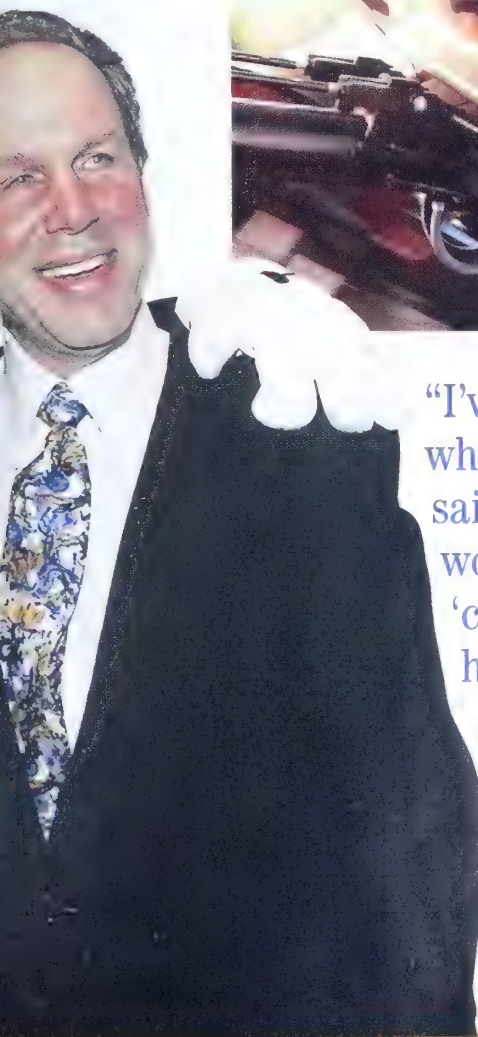
*By Ronald Grover in Los Angeles
and Gail DeGeorge in Orlando*

**ROCKETEERS: TOMORROW-
LAND'S REVAMP INCLUDES
THE "ASTRO ORBITOR"**



"I've never believed
what Faith Popcorn
said—that people
would be
'cocooning' in their
homes. People get
sick of sitting
around their
homes"

**EISNER: ADDING ANIMAL
KINGDOM, DINOLAND, AND
PLENTY OF NEW HOTEL
ROOMS**



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SPECIAL ADVERTISING SECTION

1998 SENIOR PGA TOUR Journal

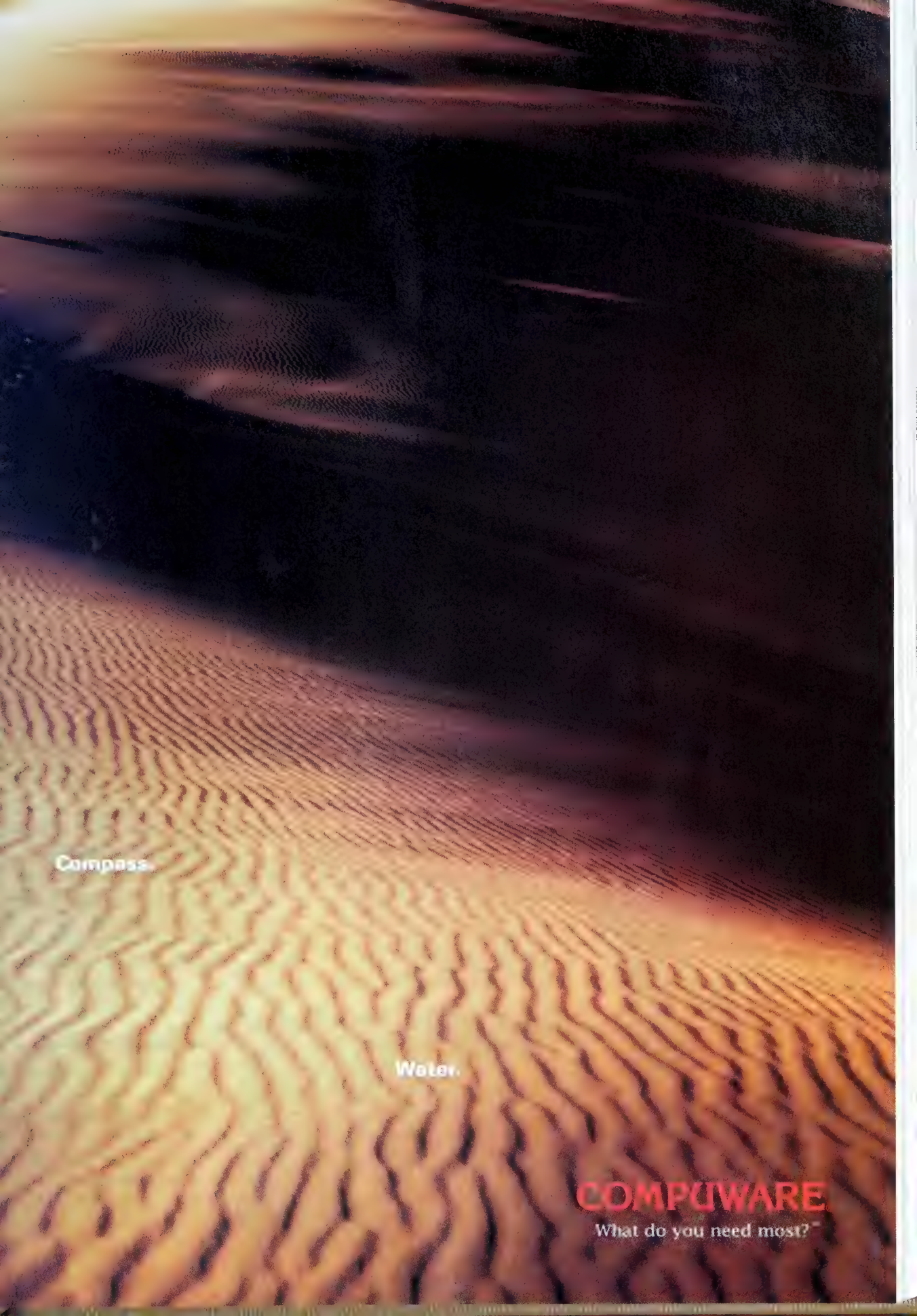
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COMPUWARE

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Cadillac

gets creative with the SENIOR PGA TOUR



From left to right: Team Cadillac members Jim Dent, Jay Sigel, Bob Charles, Tom Wargo, Dave Stockton, Bob Murphy, Jim Colbert, Arnold Palmer and Lee Trevino standing around a Cadillac Seville.

BY SCOTT GUMMER

PHOTOGRAPHY BY STAN BADZ/PGA TOUR

In this era of round-the-clock instant access information overload, it's increasingly tough to break through the clutter. This has caused companies to have to work harder to find new and better ways to reach customers. One of the best examples of creative corporate marketing is Cadillac's umbrella sponsorship of the SENIOR PGA TOUR.

Cadillac first got involved in golf 30 years ago, when it became one of two exclusive television sponsors of the Masters Tournament. The luxury carmaker has also, for years, sponsored players who serve as spokesmen through Team Cadillac, including four-time Masters champion Arnold Palmer.

Instant Credibility

Palmer's participation was key to giving the SENIOR TOUR credibility when it was just getting started. Similarly, Palmer has said, "When Cadillac became an umbrella sponsor, it gave more credibility to the SENIOR TOUR, and it attracted other sponsors because they saw a quality company involved with us." Today, the SENIOR TOUR's roster of corporate partners includes many other blue-chip corporations.

For Cadillac, the ultimate objective is to sell cars. The strategy has been to broaden the marketing mix beyond traditional media because, according to Martin Walsh, Marketing Services Manager for Cadillac, "Luxury car customers are typically active and are not the kind of people who stay home and watch traditional TV." The execution of that strategy has produced an innovative, multifaceted program encompassing title sponsorship, player participation, dealer involvement, on-site promotional activities, advertising and public relations.

Innovative Marketing

There is the Cadillac Series, a season-long competition in which players accumulate points in 22 ESPN-televised SENIOR TOUR events. A 5:30-7:00 p.m. time slot is utilized whenever possible, which means the broadcasts often air unopposed by other sports events since the networks are showing the news.



Lee Trevino

the winner of the 1998 Cadillac Series receives a Cadillac Seville STS, a 1999 Catera, while the second- and third-place finishers each receive keys to a new Cadillac. Cadillac contributes to each tournament's purse. Now in its 10th year, the Cadillac Series events have raised more than \$36 million for charity. In addition, Cadillac is the Official Car of the SENIOR PGA TOUR and title sponsor of the Cadillac NFL Classic, which features NFL stars.

But what really drives the business are the entertainment activities. "It is the perfect setting for dealers to reward their customers," says Walsh. In addition to enjoying the amenities of hospitality facilities and watching great golf, prospective buyers and loyal Cadillac customers are occasionally treated to a walk-on clinic, wherein the guests walk with a member of Team Cadillac, who plays two holes while explaining strategy and offering tips. This is always a huge hit, considering the Team Cadillac roster reads like a Who's Who of golfing greats: Palmer, Lee Trevino, Tom Stockton, Jay Sigel, Jim Colbert, Bob Charles, Bob Murphy, Tom Wargo, Jim Dent and Larry Ziegler.

Does It Sell Cars?

It sounds like a lot of fun, but does it sell cars? Indeed, since the Cadillac Series began in 1990, Cadillac directly attributes more than \$250 million in vehicle sales to its involvement with the SENIOR PGA TOUR. That's a lot of cars rolling off lots, but not too big a surprise. "People assume that because the players have to be at least 50 years old, the fans have to be over 50, too," says Cadillac's Walsh. "But the fact is the average age of spectators at SENIOR TOUR events is 45, which skews to the younger end of the luxury car market." And the fastest-growing segment of the luxury car market are buyers



of the entry-level automobile priced at around \$30,000 – about the price of a new Catera.

Looking Ahead

"Cadillac has found a home on the SENIOR PGA TOUR," said Peter R. Gerosa, Cadillac general sales and service manager, when the carmaker renewed its umbrella sponsorship through the year 2000.

"Cadillac has had a major role in increasing the popularity of the SENIOR PGA TOUR," said PGA TOUR

Commissioner Tim Finchem, when the extension was announced in 1996. "Most notably, our relationship with Cadillac has helped us develop a television contract with ESPN that allows us to bring the wonderful personalities of the SENIOR TOUR into the living rooms of millions of golf fans across the country."

The future, according to Walsh, is bright. "There are some very high-profile players becoming eligible for the SENIOR TOUR in the next two years, including Tom Watson in 1999 and Tom Kite and Lanny Wadkins in 2000. Plus, the TOUR is putting more energy into the broadcasts, discussing a variety of formats and including interactive components on the Internet."

'Creating a Higher Standard'

Log onto www.cadillac.com, and that's what it says. Tune into, or attend, a SENIOR PGA TOUR event, and you'll see it in action. Together, the SENIOR TOUR, ESPN and Cadillac have set the standard for successful sports sponsorships. ■



1998
SENIOR PGA TOUR
JOURNAL

Lee Trevino



There are some very high-profile players becoming eligible for the SENIOR TOUR in the next two years, including Tom Watson in 1999 and Tom Kite and Lanny Wadkins in 2000.



World Golf Village

Poised to Open in May



BY CHRIS SMITH
Director of Special Projects
PGA TOUR

The Slammer and The Squire golf course, which surrounds the World Golf Village property, is already being played.

Months before the final spit-and-polish phase for the May Grand Opening of World Golf Village, a newcomer to the resort's business partnership gazed around the burgeoning complex and marveled, "This is like the Land of Oz, the Emerald City."

Executive Vice President Chris Martin of W.C. Bradley Co., the Village's retail development partner, wasn't required to test his imagination to understand or appreciate this evolving dream. Unlike those who shared the vision of creating an exciting home for a World Golf Hall of Fame when this was just a barren stretch of land along Interstate 95 in northeast Florida, Martin and his colleagues had the benefit of actually seeing brick and mortar.

At one end of the Village lake, the World Golf Hall of Fame-IMAX Theater building towered over the bustling construction site. Next door, the 10-story World Golf Resort and St. Johns County Convention Center had already reached full height.

On the other side, the glistening PGA TOUR Productions

Headquarters was virtually complete and preparing for the staff's occupancy. Beyond the Hall of Fame building, the framework to the first Vistana Resort vacation ownership villas stood three stories tall. And The Slammer and The Squire golf course surrounding the Village was ready for play.

"We had the opportunity to actually see what everyone had been talking about for the past couple of years," Martin said. "To say we became involved late is an understatement."

Belated as it was, the involvement of W.C. Bradley and partner Cousins Properties Incorporated was the final, critical piece to the Village puzzle. They hit the ground running, injecting a new energy in design and philosophy to this major component of the complex.

The Shops at World Golf Village, which will open in the fall, are critical as the anchor to the end of the Village lake nearest the Interstate, across the lake from the World Golf Hall of Fame. Philosophically, they are critical in terms of broadening the World Golf Village experience through fine restaurants, interesting boutiques and the 30,000-square-foot PGA TOUR STOP, an exciting new concept in golf merchandising and entertainment. The two-story PGA TOUR STOP will feature the premier vendors in the golf industry. Brand-specific concept shops will feature 12 soft goods vendors and five equipment manufacturers, a demo-hitting area, a collectibles area and gallery, a golfers' den for home furnishings, audio and visual components, an 800-square-foot putting green and more.

Meanwhile, the Village progresses toward its public debut on Tuesday, May 19, following a private three-day celebration that concludes with a Hall of Fame induction ceremony, during which Johnny Miller and Nick Faldo will be inducted. In a state recognized for its abundance of golf courses and tourist attractions, World Golf Village is poised to become Florida's newest destination.

For those who shared the original dream and vision, being so close to the opening is both exhilarating and rewarding. Understand that the seed for what would grow into a world-class resort—home to golf's first internationally unified Hall of Fame—was planted more than a decade ago, when former PGA TOUR Commissioner Deane Beman initiated plans to establish a PGA TOUR Hall of Fame.

What evolved—first under the direction of Beman, later under his successor, Tim Finchem—were highly ambitious collaborations on two separate fronts.

On one hand was the evolution of a PGA TOUR Hall of Fame concept into the World Golf Hall of Fame, a truly international collaboration among golf's leading organizations and tours. What began with the LPGA's commitment was soon followed by the United States Golf Association, PGA of America, Royal & Ancient Golf Club of St. Andrews, Augusta National Golf Club, the major professional golf tours and other high-profile organizations. Nearly 25 organizations representing most segments of the golf industry were represented.



Photo by [illegible]

making the World Golf Hall of Fame a destination required more than simply building. So the second major initiative was finding companies willing to share the vision and risk — of establishing a major resort. As tedious as the process became at times, a proper mix was finally established. From land donation by a partnership managed 50 percent owned by cotton magnate William Dunavant of Memphis, to hotel and conference center development partner John Q. Hammons of Springfield, Mo. From EcoGroup's development of The Residences at World Golf Village, to the substantial commitment of The United Company as a venture partner in Vistana Resort and subsidiary Scratch Golf's development of three golf courses and golf academy. We saw this project through the eyes of Jim Finchem, Vernon Kelly [President of PGA TOUR Golf Course Properties] and World Golf Village Executive Director] in Beckwith, and could imagine that with the World Golf Hall of Fame and its support from all of the organizations, that this truly was going to become a world headquarters of the game itself," said United Chairman James Glothlin. "Our commitment is spread throughout the Village, because we could literally see thousands coming here who care about the game, want to learn about the history of golf rather than just read about it." Through the progression from vision to reality, other highly significant commitments were made. Shell Oil Products Company of Houston announced last May an unprecedented 20-year agreement to become the World Golf Village's Founding Partner, assuming a leading role in the charitable activities of the World Golf Foundation, which oversees the Hall of Fame and other nonprofit components of the Village. The Foundation subsequently announced its First Tee initiative to create affordable access to the game of golf for those who otherwise might not have an opportunity to play. Then came the commitment by W.C. Bradley-Cousins, plus Brassie Golf's announced partnership with Canyon Ranch Management to develop a luxury spa with retail space and executive bungalows. The World Golf Village is the centerpiece of the 6,300-acre Saint Johns Development,

a residential-business community for which Jim Davidson of Davidson Development in nearby St. Augustine is the master developer. Dunavant Enterprises, Inc., and its partner, The Cummer Land Trust, permitted the land for development in the early 1980s. The total land donation to the World Golf Village exceeds 400 acres.

"I am thrilled to see the World Golf Village and the adjacent development become a reality, after literally years of effort by the participants," Dunavant said. "In giving the land to the World Golf Foundation, the Saint Johns Project became one of the largest mixed-use developments in the country. It put Saint Johns and the World Golf Village on the map nationally and internationally."

Paramount to the success of World Golf Village was the establishment of quality accommodations, starting with a World Golf Resort Hotel. John Q. Hammons, one of the nation's premier hotel developers, stepped in with plans for a 300-room, 10-story hotel and adjoining St. Johns County Convention Center.

Complementing the hotel through rental and purchase options was the addition of Vistana Resort, a complex of upscale, one- and two-bedroom vacation ownership villas overlooking the finishing holes of "The Slammer and The Squire" golf course.

"This project has taken the vision and hard work of world-class organizations, and we are proud to be a part of the World Golf Village Team," said Raymond Gellein, Jr., Chairman of the Board for Vistana Development, Ltd.

Finally, there was EcoGroup's The Residences at World Golf Village, luxury three- and four-bedroom condominiums geared for executives and families, featuring a conference center, pools and tennis courts.

Once the festivities of May 16-18 subside, the gates to World Golf Village will open to the public. The World Golf Hall of Fame and Museum rightfully will be celebrated as the centerpiece to this amazing project, educating and entertaining hundreds of thousands of visitors with memorabilia and interactive displays in the coming months.

But the underlying success of World Golf Village rests with those who, long ago, bought into a vision when there was little more to see than pines, scrubs and wetlands along I-95. ■



1998
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JOURNAL



Hall of Famer Sam Snead

**For those who
shared the original
dream and vision,
being so close
to the opening is
both exhilarating
and rewarding.**

The All New Chrysler Concorde

Once again,
we've successfully
avoided
the pedestrian.



Well-equipped from \$21,855*

There are a lot of words that can be used to describe the all-new Chrysler Concorde. "Pedestrian" is definitely not one of them. In fact, the new Concorde stands as an exhilarating testament of our engineers' relentless commitment to inspired

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C H R Y S L E R



E N G I N E E R E D T O B E G R E A T C A R S



MasterCard Champions

Dale Douglas

BY HARLESS WADE

PHOTOGRAPHY BY STAN BADZ/PGA TOUR



They are old enough to accept

senior-citizen discounts and

resorts for the aged, yet the

great grandfathers of the

PGA TOUR may be having

more fun now than in their

childhood. When they

could jump a four-foot creek

without needing to dial 911

SECTION

Thank you, say the men battling for bucks along the MasterCard Champions trail on the SENIOR PGA TOUR. Sure, they've got to be at least 60 to compete, but they're not ready to settle into a rocking chair yet.

One of those leading the MasterCard Champions is "Ol' Bones," Don January. Now 68, lanky and raw-boned, he still looks more like a Texas cowboy than John Wayne or Randolph Scott.

The enjoyment level may be even greater around the January household today than it was when he kicked off his career before the homefolks with a victory in the 1956 Dallas Centennial Open. Or when he joined the major championship winners at the 1967 PGA Championship.

"Thankfully, what goes around comes back around," said the six-time grandfather during a night session with an old friend. "I've been most fortunate. It's wonderful to be having so much fun at our age."

A Perk for the 60-And-Over Set

Although at 60 Charles Coody is nearly a decade younger, he couldn't agree more with January. "This is my third time as a rookie on tour, from the PGA TOUR to the SENIOR TOUR to the MasterCard Champions," said the 1971 Masters champion. "And it's great to have a perk like this. I know it's a tremendous thing. I'm just a rookie and loving it."

The MasterCard Champions schedule has stretched career life for more than just yesterday's superstars like Billy Casper and Gene Littler. It has helped create new careers and riches for the likes of former steelworker Walt Zembriski, stockbroker John Paul Cain and municipal club professional Jimmy Powell.

Powell left Stevens Park Municipal in Dallas and joined the SENIOR TOUR in 1985. He has collected more than \$3.33 million since, including the \$284,004 he won at the 1997 MasterCard Champions.

January and Powell attended the same high school in Dallas. Between them, they have given Sunset High two of the biggest winners in MasterCard Champions competition. January is the all-time leader with a record 35 titles in the unofficial money competition. Powell owns 17, and he became the first 60-and-over player to win both the

sterCard Champions and tournament
es at the 1995 First of America Classic.
The MasterCard Champions covers just
first two days of a three-round SENIOR
UR event, but players also compete to
the regular 54-hole event. Along with
vell, Bob Charles and Dale Douglass also
re "double-dipped" a tournament, each
1996, when Charles won the Hyatt
gency Maui Kaanapali Classic and
uglass captured the Bell Atlantic Classic
er winning the MasterCard Champions.
at same year, Powell won both titles again
the Backyard Crossing Championship.
d 61-year-old Bruce Crampton won the
7 Cadillac NFL Golf Classic, where there
no MasterCard Champions competition.
Coody, who captured the year-ending
7 MasterCard Champions Championship,
eves he still has as much "fire in the belly"
he did when he first joined the PGA TOUR.
"In my mind I do, but the hard part is
king at the statistical records. Then it
comes obvious we're not at the same
npetitive level as the younger guys,"
d Coody. "But at 60, we're playing those
our age bracket, so we're competitive."
January, who claims 75 worldwide profes-
sional titles, including those 35 MasterCard
ampions, once interrupted his 42-year
eer for 30 months to construct golf courses.
ecession in the early 1970s forced him
k on the PGA TOUR in 1975.
It was a dynamite return: he won twice.
A year later, he picked up the coveted
don Trophy at age 46 with a 70.56 scoring
verage. It prompted him to say he would
leave the TOUR on his own again. He
quietly stuck by those words.
One of six founding fathers of the SENIOR
UR, January is a walking history book on
v it all came about. Since that first major
eting in the late 1970s with Sam Snead,
rdner Dickinson, Dan Sikes, Julius Boros
d Bob Goalby, he has seen the SENIOR
UR grow beyond his wildest dreams.
"Back then, I don't think anyone could
ve visualized what has happened," said
January. "We didn't want to be just another
g-and-pony show, but we were sort of
instorming it in the beginning. We were
ping to come up with 10 or 12 tournaments.
w look what we have."



Don January

During talk of those early days, January, who was nicknamed "Bones" by his TOUR mates years ago, was a bundle of chuckles, like when he recalled what Boros would say. "He would tell us he didn't really care how many events we could get, he just wanted to get out of the house 10 or so times a year."

"Bones" has stuck on January out on the SENIOR TOUR, just as growing old has created more aches and pains.

A Pain In The Neck

Coody also laughs about the squeaks of growing older. "I didn't believe it when the older guys would tell me about it, but now I know," he said. "Every morning it's something different—a bruise, a little soreness or a pain in the neck."

Thus far, Coody's biggest health problem has been just that: a pain in the neck. That's more fortunate than a lot of his friends on the SENIOR TOUR. Fans and SENIOR TOUR mates alike marvel at the toughness of any number of players who have fought off major health problems to keep on making birdies and bogeys.

Gene Littler, Arnold Palmer, Jim Ferree and Jim Colbert are among those who have battled cancer. Bruce Devlin had a cancerous kidney removed last year. George Archer, the SENIOR TOUR's Comeback Player of the Year for 1997, plays with an artificial hip and a five-inch steel rod in his back. And Bobby Nichols underwent double-hip surgery in 1996.

Do the old players suffer more than the young ones when they shoot a bad round?

"I don't think Don ever let it bother him too much," said Pat January, Don's wife of 42 years. "He's always had a good attitude about that. With him, it's always been that tomorrow is another day."

Don agrees, reliving what happened to him when he was in position to win going into the final round of the third event of 1998, the LG Championship in Naples, Fla.

"The guy who shot those first two rounds (72-72) is the same guy who shot 78 on Sunday," he said.

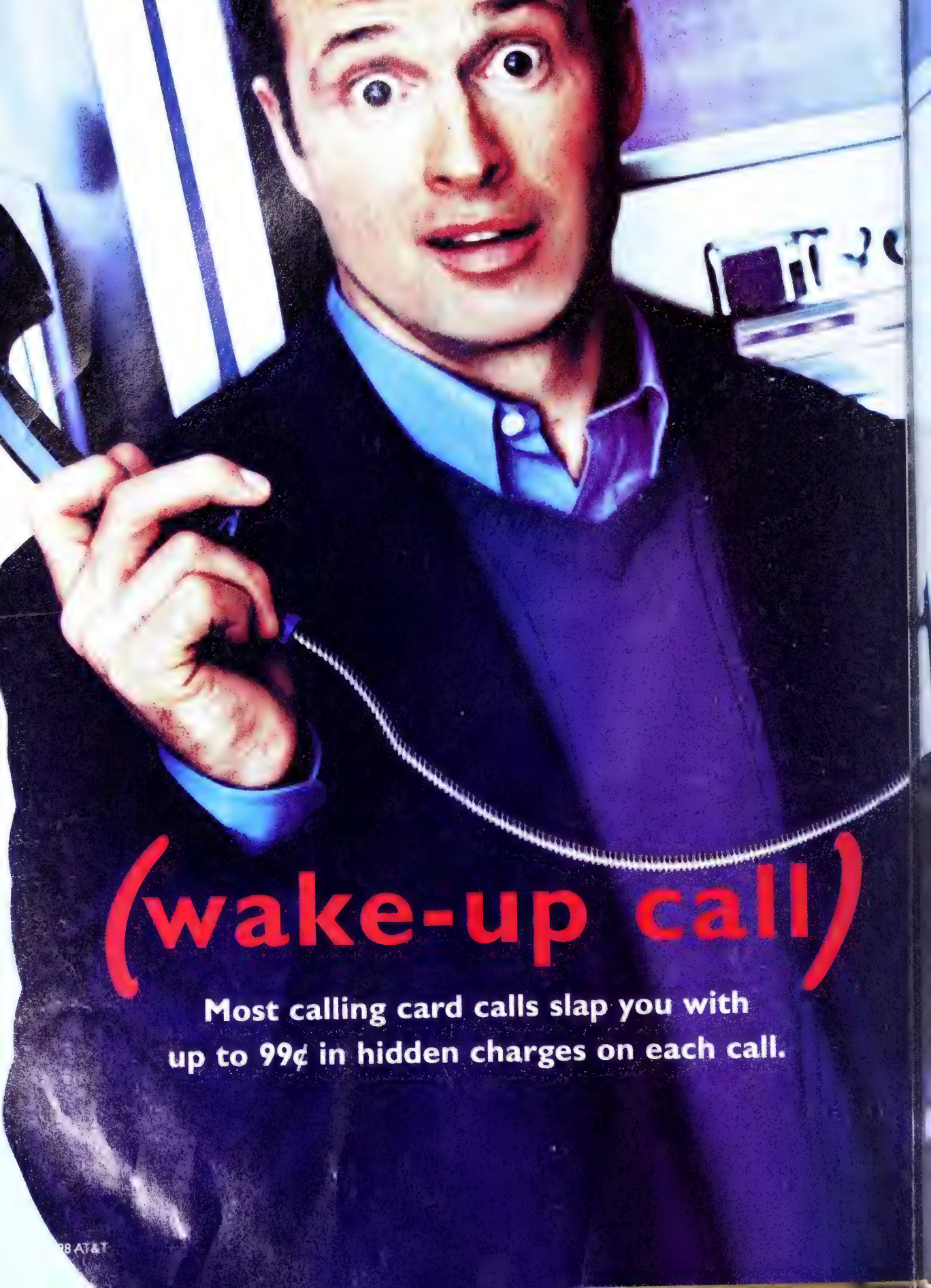
But January laughed when he said it. For the 60-and-over bunch, that's what makes the MasterCard Champions so sweet. ■

1998
SENIOR PGA TOUR
JOURNAL

**Fans and SENIOR
TOUR mates alike
marvel at the
toughness of any
number of players
who have fought
off major health
problems to keep
on making birdies
and bogeys.**



Bruce Crampton

A man with a shocked expression, wide eyes, and an open mouth, holding a telephone receiver. He is wearing a dark sweater over a light blue collared shirt. The background is slightly blurred, showing what appears to be a kitchen or office setting.

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AT&T

What's Driving Golf Today?

BY REID HANLEY

PHOTOGRAPHY BY STAN BADZ/PGA TOUR



At the rate the size of drivers is increasing, players on the SENIOR PGA TOUR might need to hitch trailers behind their golf carts to carry them. The oversize driver is in the bag of almost every player on the SENIOR TOUR. Whether it's a Taylor Made Ti Bubble 2, a Cobra Ti, a Top Flite Intimidator, a Goldwin AVDP, Callaway's Big Bertha, Gary Player's Black Knight, a Ping ISI or whatever, it's big and bad.

The advent of the oversize driver has sent golfers to Acme Tent and Awning for head covers. It's hard to see the ball in the shadows cast by these monster-sized clubs. Is there no end to this "bigger is better" revolution?

Twenty years ago, persimmon was the wood of choice and heads were about 150cc in size. When the first metal woods became the rage almost two decades ago, it opened up a new frontier in golf equipment. The move to big—200cc range; bigger—250cc range and biggest—300cc range was a natural progression. The reason for their popularity is simple: they work.

"There is only one factor, and that has to do with performance," said Johnny Miller, former U.S. Open champion, television analyst and sometime SENIOR TOUR player. "Guys who play on a professional level will use anything if it works better. And oversize drivers work better."

The oversize driver was designed for the average player, not the SENIOR TOUR player. It didn't take companies long to realize, after talking to SENIOR TOUR players, that these clubs were for everybody.



SENIOR TOUR Sets Trend

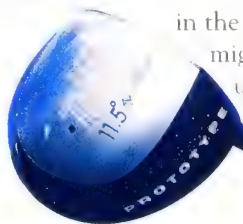
"The SENIOR TOUR made the big-headed driver popular," said Gary Player, who was a clubmaker when he first turned professional. "Before, we never had the opportunity to play with square grooves, lightweight shafts, light grips or big heads. When we see something like the big driver, we say, 'Let's try it.' Change is the price of success."

With the bigger clubhead comes a bigger sweet spot and a bigger margin for error. There is an increase in distance and an even bigger increase in accuracy. Titanium is strong enough and light enough to allow the driver heads to exceed 300cc, dwarfing the traditional driver.

"I wasn't shocked when I saw the first big-headed drivers," said Player. "Look at tennis with the big racquet. It makes sense. Now the average player can tee the ball high and have confidence. The big drivers have made it easier all around."

An even bigger head might not be possible in titanium, and other metals might be too heavy. Also, aerodynamics will come into play at some point. While current materials might dictate the end of the size race, there are other considerations. With the original oversize clubs, there was a period of adjustment to the look of the club. Now, with a driver in the 300cc range, the golf ball looks

mighty small when teed up. Even bigger might not be better. ■



Bruce Summerhays



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Tips from the

SENIOR PGA TOUR

BY BOB HARIG WITH GEORGE ARCHER

PHOTOGRAPHY BY STAN BADZ/PGA TOUR

There have been so many injuries over the years that George Archer is running out of fingers to count them. The tally for major surgeries is seven, and the latest one nearly forced him to retire.

Archer's right hip was giving him so much pain two years ago that he considered leaving a game he has played so well for some three decades. He won twice on the SENIOR PGA TOUR in 1995 despite the degenerative hip condition that finally forced him into surgery in April 1996.

The right hip was replaced, and although Archer competed on only a limited basis in 1996, he came back for a full schedule last year, playing in 26 tournaments and posting five top-10 finishes. He saved his best performance for last, shooting a 64 in the final round of the Ralphs Senior Classic to finish one stroke behind Gil Morgan. For his inspired play in 1997, Archer was voted SENIOR PGA TOUR Comeback Player of the Year by his fellow players.

Throughout his career, Archer, 58, has always been known as one of the game's best putters. That helped him win 12 times, including the 1969 Masters, on the PGA TOUR. He has added another 17 SENIOR TOUR titles. At one time, he held the TOUR record for fewest putts over four rounds when he had 95 at the 1980 Heritage Classic.

But bunker play was always a continuing study. "You have to work hard, practice and get confident," Archer said. "I became a good bunker player, a much better bunker player, after I found out what worked for me."

"Many players fear the sand because they don't understand the shot. Fear is your worst enemy in golf. You have to understand and know how to play a sand shot. So many people will take lessons to hit a golf ball,

but never take lessons on how to get out of the sand."

Archer stresses that there is no simple solution to hitting good bunker shots.

"There are a lot of different ways to do it," said Archer, who led the SENIOR TOUR in sand saves in 1992 and 1993.

"If it's a long shot, you want the ball to carry and roll. Sometimes you have to get the ball to stop really quick. Those are the hardest, and they are played completely different."

"There are a lot of different styles. Some people cut across the ball, some people use more of a shovel



style. It's hard to talk about touch and feel in words. You have to develop your own touch and feel."

With that said, Archer addressed several aspects of bunker play:

STANCE: "It's all determined by the lie. But if it's a normal shot, you want to have a bit of an open stance. The shorter the shot, the more I open my stance."

GRIP: "The shorter the shot, the weaker I make my right hand. In other words, I turn it over to the left. If I want to hit a real short shot, I turn the right hand way over. The right hand keeps the blade from going shut. On a short sand shot, you don't want the blade to shut. It forces the blade to stay open the whole way."

FORCE: "When I wasn't a very good bunker player, if I had a short shot, I would try to ease it out. And I would hit the ball too far. That's when I learned the trick with the right hand. By moving the right hand way over [to the left], I could hit the ball harder, but still hit a very short, very up and down shot."

CLUBFACE: "The shorter the shot, the more I want the clubface open. And I'm not hitting the ball easy. I'm swinging harder. When you're nervous, you never want to hit it easy. You want to hit the ball firm."

HITTING BEHIND THE BALL: "This depends on how far the shot is. You have to really know what you're doing, what you can do and what you can't. A good rule of thumb is the longer the bunker shot, the closer you hit behind the ball. If it's a long bunker shot, I'll hit the ball first. That's what you do when you need to take a full swing out of the bunker."

Archer also has some extra advice for those players who are new to the game and just content to get the ball out of the sand and somewhere on the putting surface.

"You need to learn how the sand club works," Archer said. "What the principle behind it is. Gene Sarazen invented the sand wedge when he realized that a club with bounce would help get the ball out of the sand. For beginners, getting a club with bounce will give you confidence to get the ball out." ■



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Tips from the

SENIOR PGA TOUR

BY BOB HARIG WITH JOHN JACOBS

PHOTOGRAPHY BY STAN BADZ/PGA TOUR

Golfers have a fascination with the long ball. No matter what their proficiency level, players always seem to want to hit the ball farther. And that helps explain their infatuation with those who make smacking the ball into orbit seem so effortless.

John Jacobs is one of those players. He hits ball after ball out of sight on SENIOR PGA TOUR driving ranges. And he does so with stunning ease. In fact, winning the driving title is important to him. "It is a pride thing," Jacobs said. "I'm the longest hitter, so I should win it."

Jacobs led the SENIOR TOUR in driving distance in 1997, averaging 290.7 yards per tee shot. His longest measured drive of the year was 378 yards. And his ability to hit the ball far has translated into birdies. He converted more par-five birdie opportunities than any other player (175 of 385, or 45.5 percent).

Some might say that Jacobs has a few built-in advantages to hitting the ball far. He is 6-foot-3 and 225 pounds, which gives him a powerful base from which to generate clubhead speed. But Jacobs also was blessed with the opportunity to watch the game's best when he was young: He once caddied on the PGA TOUR.

"When I was 15, I caddied one summer for Tony Lema," Jacobs, 52, recalled. "I got to see guys like Gene Littler play. I saw how the good players swing. And there is one thing I noticed: anyone who played well or lasted a long time had a big shoulder turn. That has always stayed in my mind."

Jacobs, who had 12 top-10 finishes and earned \$802,942 to rank 12th on the SENIOR TOUR money list in 1997, sees many flaws in pro-am players who are unable to hit the ball a long distance. For some, their body is too stiff at impact. Others get no weight on their left side. Or they

might swing entirely with their arms.

"That's one thing about a lot of these seniors: these guys can still play because they're working out and keeping their flexibility," Jacobs said. "You just cannot function without a shoulder turn. Look at some of the guys who have lasted for years, guys

like Al Geiberger, Gene Littler, Don January. They've all got the big shoulder turn, the big, lazy swing." Jacobs has several key points to driving the ball long.

PLANT YOUR RIGHT FOOT: You want your right foot to be a solid base. "Then I take my sternum, the center of my chest, and make a big shoulder turn," Jacobs said. "When I come down, I push off as hard as I can from my right side and hit against a firm left side. It's almost like a boxer. When he throws a punch, he punches against his left side. He doesn't fall over his left side. It's the same thing with hitting a golf ball."

TAKE A LIGHT GRIP: "If you tense up your grip, then it goes right up your arms," Jacobs said. "Your forearms get tight and so do your shoulders. That goes right through your mind. You need to relax. And if you're into the wind, you have to take an even lighter grip and concentrate more on that big shoulder turn. If you grip the club too tight, you won't have the flexibility to turn. You almost want to swing easier. Most people tense up when they don't trust their swing. If you trust what you're doing, you won't tense up."

FLEX YOUR KNEES: "Most amateurs hit with their legs straight," Jacobs said. "At impact, they're not bent at all. They've got no flex. It's actually better to flex down farther and come back up than to be so straight up."

TOUCH YOUR SHOULDER: "To get the proper turn, I try to think of hitting my left shoulder to my chin. Then I know I've turned enough," he said.

FINISHING THE SWING: "If you're not up on your left side looking at the target, you haven't made a very good swing," Jacobs said.

KEEP IT SIMPLE: "Plant your right foot, turn your sternum, swing and push off with the right foot. Finish facing the target," Jacobs said. "With most of the guys who hit it long, you don't necessarily see a big, long swing. But you need a big shoulder turn."





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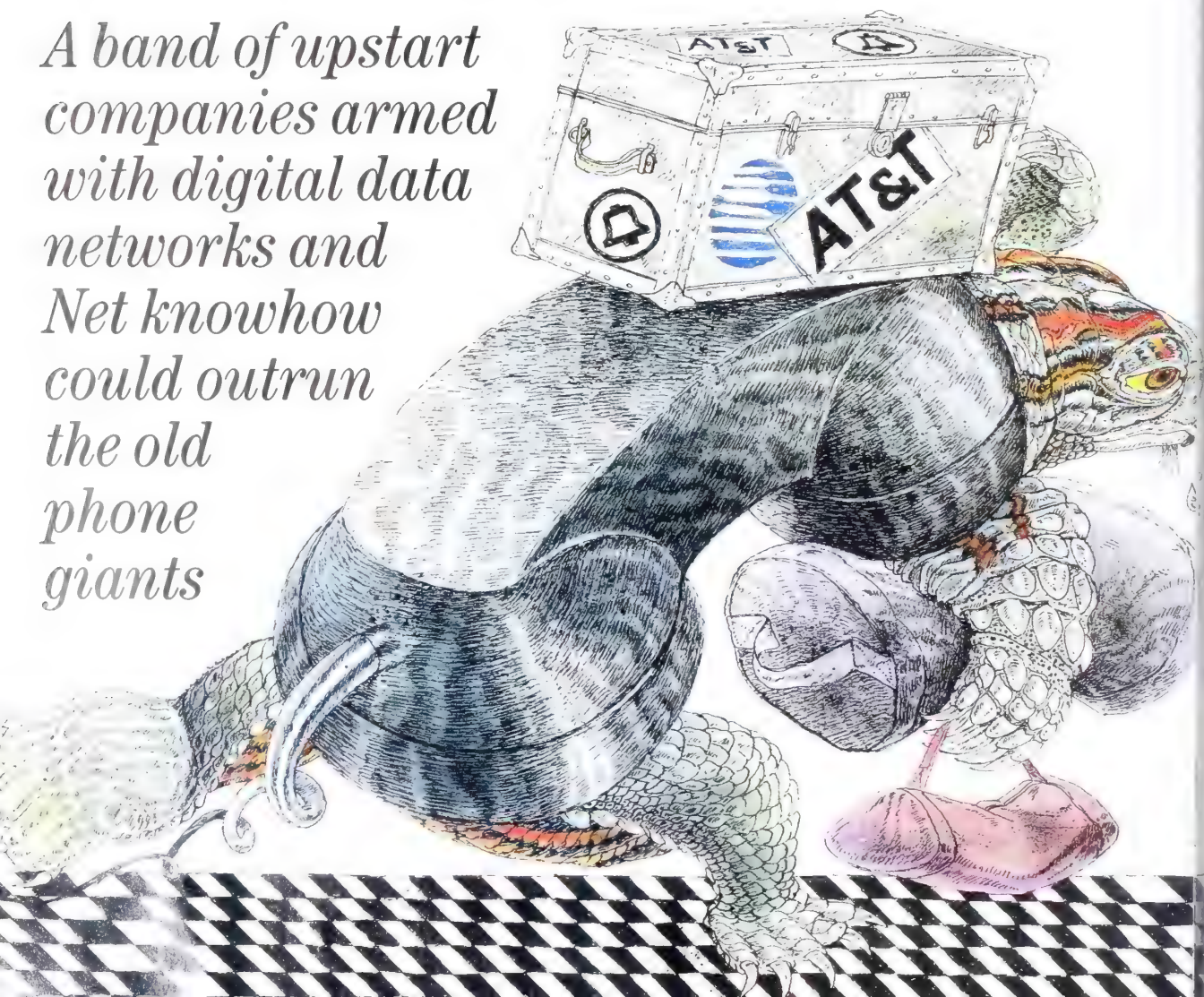
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The New **TRAILBLAZERS**

A band of upstart companies armed with digital data networks and Net knowhow could outrun the old phone giants



ell-heads beware. In the high altitudes of Denver, the back roads of Tulsa, and the swamps of Mississippi, a band of maverick companies is popping up—and neither the \$600 billion telecom industry nor your phone service will ever be the same. Qwest Communications International Inc. is now long distance for 7.5¢ a minute. A company called IDT will charge you a mere 5¢ a minute, or one-third of popular One Rate plan. And you end an international fax for 65% than the going rate if you go to lit-tle-known providers such as UUNET Technologies Inc.

These upstarts, with no ties to the world of Ma Bell's monopoly, are building telecom networks from scratch and taking advantage of the computer industry's whizzy technology and potent economics. Companies such as Qwest, MCI Telecommunications, and Sprint Communications Cos. are laying fiber-optic cables and using Internet technology to build faster, cheaper systems than old telephone networks. These new digital lines swap information seamlessly with each other. And by converging voice, data, and video on the same line, they can offer snazzy new services—such as integrated voice mail—not currently possible elsewhere. "They're scaring the heck out of the big companies," says analyst Adamik of market researcher Group Inc.

There's good reason. This could be the dawn of the next-generation telephone service. Just five years ago, these upstarts were little more than niche players, hawking data networks to trans-computer and Internet traffic. Now, data networks are catching on as the best way to handle voice calls, too. And the super-efficient lines carry less than 1% of the total voice traffic. But within four years, experts say, that could reach 13%. "This really challenges the fundamental assumption of the industry," says Mark Winther, International

Data Corp.'s group vice-president for worldwide telecom.

To be sure, the upstarts have much to overcome before they reach titan status. Traditional phone companies still claim nearly all the customers—their revenues are 50 to 100 times greater than the \$400 million average of the newcomers. And the giants have plenty of cash to acquire the troublemakers if need be. SBC Communications Inc. Chief Executive Edward E. Whitacre Jr. has floated the idea that the

Bell could buy a company with a converged network, such as Denver-based ICG Communications or Tampa-based Intermedia Communications Inc.

Then again, the old guard could simply build converged networks themselves. "They haven't created the formula for cold fusion. They can't buy equipment we can't buy," snaps Brian A. Brewer, senior vice-president at MCI Communications Corp.

No, but they can shake things up. Already, Wall Street is betting on the new generation: Today, these companies are valued at 10 times their revenues, vs. traditional phone companies at two times revenues. One telling example of the new balance of power came on Mar. 9, when Qwest agreed to acquire LCI International Inc., the country's fifth-largest long-distance company, for \$4.4 billion in stock. LCI CEO H. Brian Thompson explained why he sold out to a company with less than half the \$1.6 billion in revenues LCI has, saying: "That's just a function of market caps." Qwest's market capitalization of \$8 billion is more than twice LCI's.

Even if the new Telecom Turks should stumble or are snapped up by the majors, the looming shadow of their success will force the giants to change their ways. That will trigger deep, structural changes throughout the industry—from pricing and new services to throwing up for grabs which companies will be the dominant phone carriers and telecom-equipment suppliers into the 21st century.

The initial impact: Buzzsaw competition that could bring

NACCHIO'S REVENGE

An ex-AT&T exec turns Qwest Communications into a star **96**

TULSA GUSHER

How telecom is energizing gas-pipeline operator Williams **97**

BELL-BEATER?

Level 3 is using the Net to deliver dirt-cheap communications **98**

PICTURE PERFECT

Ford breaks new ground with converged networks **100**

AND IN THIS CORNER...

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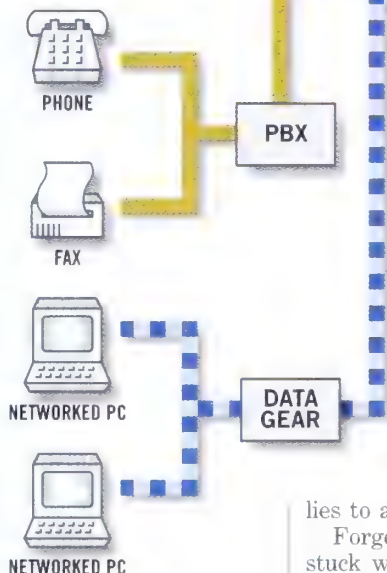
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In homes, telephone calls, faxes, and Internet connections are made one at a time over a circuit-switched line.



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In businesses, calls are usually handled by a Private Branch Exchange (PBX), which bundles and sends them to the local phone company on pricey, high-capacity trunk lines. These lines typically handle 24 voice circuits. From the local company, calls are sent to local and long-distance numbers. Data, such as from one PC to another, are lumped together by networking gear and sent in packets over data lines to the local phone company.



TRADITIONAL NETWORKS use an entire telephone channel for every phone call, fax, or data connection, and route the call from sender to receiver by establishing a single end-to-end circuit. That's why they're called "circuit-switched" networks, the equivalent of a driver reserving a whole lane on a highway trip between New York and Chicago.

prices tumbling down. In part because of pressure from the newcomers, U.S. long-distance rates are projected to fall by a third over the next two years. International and fax rates are likely to drop even further—as much as 50%. That will leave traditional long-haul carriers fighting over a shrinking pie: The old phone networks will carry \$77 billion in U.S. long distance in 2002 because of drastic price cuts, down from \$83 billion last year, according to IDC.

CONVERGENCE. But lower prices will seem insignificant compared with what's ahead: The features that come with telephone service are set to flourish as traffic shifts to converged networks and the ability to develop applications opened up beyond a handful of former monopolies.

lies to a whole new world of computer-industry inventors.

Forget Caller ID. In the next three years, consumers, not stuck with old twisted pair phone lines, could start to have their connections go digital. As that happens, it will throw open the door to space-age phone options. Consumers might be able to ask their telephone who's calling, and, thanks to speed recognition software and the converged networks, it will tell them. A pricey video screen for viewing your old college chum while chatting would suddenly be affordable.

But it's businesses, which already have high-speed data networks, that could go hog wild. Hotel operators could talk to potential customers while simultaneously showing them the views from various rooms. United Parcel Service of America, Inc., for example, is developing a way for customers trying

to track a package at UPS's Web site to speak to a live operator over the same line. "What we can think of is only the tip of the iceberg," says Thomas Evslin, a former AT&T executive who now runs IXTC Corp., a North Brunswick (N.J.) company that provides services for the new networks.

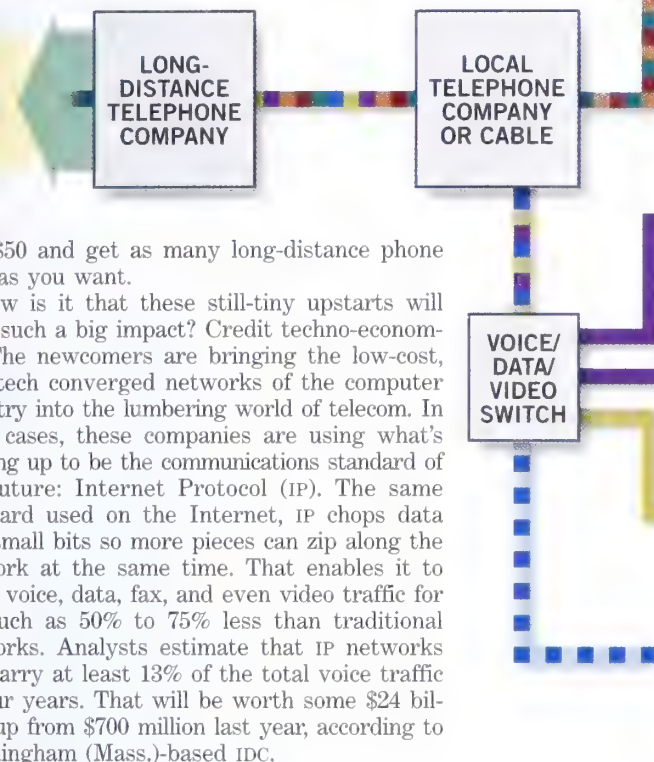
How you pay for service will change, too. If your teenagers are monopolizing the phone, you won't have to go through the expense of getting a second telephone line. Instead, you'll order more bandwidth so you can handle multiple calls over one line. You will even stop paying for calls by the minute—the so-called death of the minute. Instead, perhaps as soon as three years from now, you could opt for a flat monthly fee

Special Report

TELECOMMUNICATIONS



GED NETWORKS combine voice calls, data, and even of video onto a single line. All these different re chopped into chunks of data, or "packets"—the hey're called "packet-switched" networks. It's the ent of letting many cars travel in each lane of a . These networks also make more efficient use of way: While traditional voice calls use a channel 64 wide, the most common packet-switched network ses voice to 8 kilobits.



In homes, new devices such as cable modems and Digital Subscriber Line modems will allow voice and data calls to share a single connection to the local carrier.

\$50 and get as many long-distance phone as you want.

Now is it that these still-tiny upstarts will such a big impact? Credit techno-econom- the newcomers are bringing the low-cost, tech converged networks of the computer try into the lumbering world of telecom. In cases, these companies are using what's ng up to be the communications standard of uture: Internet Protocol (IP). The same ard used on the Internet, IP chops data small bits so more pieces can zip along the ork at the same time. That enables it to voice, data, fax, and even video traffic for uch as 50% to 75% less than traditional orks. Analysts estimate that IP networks arry at least 13% of the total voice traffic ur years. That will be worth some \$24 bil- up from \$700 million last year, according to ingham (Mass.)-based IDC.

LEADER. The success of the converged orks may not stop there. Several industry experts pre- hat all the calls that now run over the U.S. phone m will switch over to the new networks in as little as 10 years. "No question about it," says Eric A. Benhamou, of network-equipment maker 3Com Corp. Frank Ianna, AT&T executive vice-president responsible for keeping its ork up to date, also sees big change ahead. "Certain car- may get nailed," he says. "The paradigm switch may them sleeping."

AT&T doesn't plan to be one of the ers. The giant carrier is probably ost vulnerable to the technology because it holds the lion's share long-distance, international, and raffic. It also has the highest ead in the industry—29% of rev- . AT&T has a hard time matching rices of MCI and Sprint, much hose of the next generation.

t new CEO C. Michael Armstrong ermined to change that. To be- ore competitive, he's cutting 18,000 jobs to reduce overhead

to 22% within two years. At the same time, AT&T plans to of- fer a version of IP voice through its WorldNet Internet-access business this spring.

And it's upgrading its network to prepare for the Digital Age. By yearend, the long-distance giant plans to have com- pleted a new network of 55 fiber-optic rings throughout the country. While the rings carry mostly traditional voice traffic now, they will be able to carry data packets with the installa- tion of new electronics and photonics. Advances in technology will expand the capacity of those rings fivefold by next year, the company says. "I don't know about the other carriers, but AT&T is sure as hell getting ready for this," says Ianna.

Count MCI among the believers, too. The long-distance carrier is devoting 50% of its capital expenditures to converged networks. That has helped it develop a proprietary technology called Vault that helps old networks share traffic with the new ones. "We take Qwest and [the others] very seriously," says MCI's Brewer.

What makes all-in-one networks so important strategically is that the tech- nology allows carriers to cash in on the



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To: Everyone who contributed
Subject: A job well done.

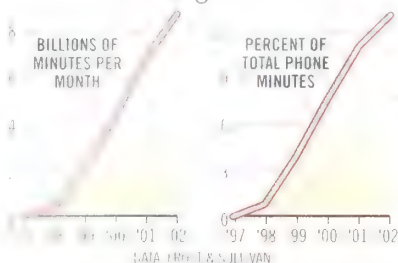
Microsoft® Office 97 encourages cooperation among teams by giving credit where credit is due. As everyone works on a document or project, they're free to exchange ideas and information, all electronically. Expressing opinions, revising the wording, proofing the copy, adding sections, inserting hyperlinks—they're all recorded with the original document, and everyone's got their name on them. If you're in charge of the project, you're in control. Use the comments you like and toss the ones you don't, knowing who contributed what, when and why. You don't have to retype anything; you revise as you go. You don't have to save a new version for each round of changes; you only save the changes. Then you just say, thanks for the help, guys. For more help, and to find out about the free* online product enhancements and assistance available through Microsoft Office Update, visit www.microsoft.com/office/.

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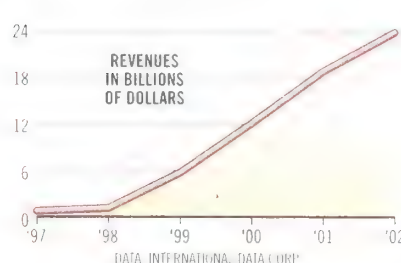
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explosion in data traffic at the same time they're carrying voice calls. Traditional phone systems simply aren't very good at transporting data. They were built for three- or four-minute phone calls, and 30-minute connections to the Net clog up their capacity. The result: Voice traffic is growing about 8% per year, while data traffic is soaring 100% annually. "Five years from now, data is going to be the dog, and voice is going to be the tail," says Richard Christner, vice-president at New York-based Mercer Management Consulting Inc.

Surging Voice Traffic Over Converged Networks...



...Promises Fast-Growing Revenues



as consumers and businesses demand lower costs and better-integrated voice and data services. They also have stepped up the pace of acquisitions. Telecom companies that have taken years to roll out services, such as voice mail or Digital Subscriber Lines, will find high

tech rivals bringing new products to market every few months.

Most traditional telecom companies are vulnerable. Consider how the next-generation phone companies are poised to wreak havoc in several of the old phone players' most lucrative markets, especially fax, long distance, and international calling. ICG Communications Inc., for instance, expects to offer long-distance service for 5.9¢ a minute in 238 U.S. markets by the end of the year. AT&T and others may not have a match that rate, but experts say they will be forced to cut prices. "What happens to them when they can only charge

Special Report

TELECOMMUNICATIONS

That presents tremendous challenges for the traditional U.S. phone companies. The infrastructure the titans have spent a century building may turn from assets into anchors

The Telecom Giants

Telecommunications may be a booming business these days, but a look at the largest widely traded service providers and equipment makers shows that the boom is no guarantee of big profits

COMPANY (TICKER SYMBOL)	1997 SALES BILLIONS	CHANGE FROM 1996 SALES	1997 NET INCOME BILLIONS	CHANGE FROM 1996 NET INCOME	MARKET VALUE BILLIONS	ONE YEAR RETURN	THREE YEAR RETURN
NIPPON TEL. & TEL. (NTT) ■ *	71.1	-4.6	2.0	-21.5	67.6	28.4	5.4
AT&T CORP. (T) ■	51.3	-1.7	4.6	-21.5	106.6	85.9	NA
DEUTSCHE TELEKOM AG (DT) ■	40.6	-11.9	1.1	-69.2	62.8	1.7	NA
BCE INC. (BCE) ■	33.2	17.8	1.4	22.7	25.3	66.5	44.3
ALCATEL ALSTHOM CGE (ALA) ●	31.2	-2.6	0.5	110.3	24.7	40.3	25.7
BELL ATLANTIC CORP. (BEL) ■	30.2	130.8	2.5	41.2	76.8	58.3	27.4
MOTOROLA INC. (MOT) ●	29.8	6.5	1.2	2.3	32.7	1.6	-0.2
FRANCE TELECOM SA (FTE) ■	29.4	-2.6	1.9	5.9	57.1	NA	NA
LUCENT TECHNOLOGIES INC. (LU) ● +	26.4	13.2	0.5	NA	77.9	108.5	NA
SBC COMMUNICATIONS INC. (SBC) ■	24.9	78.8	1.5	-29.8	73.5	51.8	28.4
TELECOM ITALIA SPA (TI) ■	24.2	2.4	1.0	-33.3	10.7	62.8	NA
BRITISH TELECOMMUNICATIONS (BT) ■ *	24.1	8.8	3.3	10.0	66.9	72.6	32.2
GTE CORP. (GTE) ■	23.3	9.0	2.8	-0.1	54.9	29.3	24.1
ERICSSON AB (ERIC) ●	21.2	15.2	1.5	45.1	41.4	36.3	48.2
BELLSOUTH CORP. (BLS) ■	20.6	8.0	3.3	14.2	61.3	48.8	32.8
MCI COMMUNICATIONS CORP. (MCIC) ■	19.7	6.3	.002	-99.8	27.4	29.9	32.8
AMERITECH CORP. (AIT) ■	15.9	7.2	2.3	7.6	51.4	55.1	33.4
NORTHERN TELECOM LTD. (NT) ●	15.5	20.3	0.8	33.1	31.8	79.8	53.6
TELEFONICA DE ESPANA SA (TEF) ■	15.3	7.2	1.2	11.9	38.3	73.7	57.6
SPRINT CORP. (FON) ■	14.9	5.9	0.9	-19.8	24.0	64.5	NA
TELECOMUN BRASIL-TELEBRAS (TBR) ■	12.3	38.7	2.6	217.0	25.1	24.9	NA
TELSTRA CORP. (TLS PP) ■ †	12.1	0.8	1.2	-32.6	33.3	NA	NA
U.S. WEST COMMUNICATIONS GROUP (USW) ■	10.3	116.3	1.2	-2.9	26.5	70.7	NA
CA & WIRELESS PLC (CWP) ■ *	9.7	15.6	1.1	17.6	27.2	55.7	27.5
NOKIA CORP. (NOK.A) ●	7.7	-9.0	0.6	74.5	31.5	69.0	41.6

■ = Telephone carrier, ● = Equipment maker, * = Fiscal year ended March, + = Fiscal year ended Sept., † = Fiscal year ended June

Business For a listing of the top 100 telecom companies, with detailed financial information, see the Business Week Web site www.businessweek.com

DATA: STANDARD & POOR'S FINANCIAL INFORMATION SERVICES

POSTAL EMPLOYEES HAVE TURNED THIS INTO THE SYMBOL FOR CUSTOMER SERVICE.



The American people have awarded the Postal Service an unprecedented honor.

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Service accountable, credible, competitive – a compelling choice in communications.



We deliver.

There's Life After AT&T—and How



It got really nasty two years ago when Joseph P. Nacchio left AT&T. After criticizing then-CEO Robert E. Allen's business strategy, the phone company's head of consumer operations found himself muzzled in high-level meetings and desperate to make a getaway. "You don't expect a callous attitude as if you're in grade school, where you can comment only in a limited way," the hard-charging New York native recalls. Adding injury to insult: AT&T tried to deny Nacchio millions of dollars in benefits when he left.

Now, Nacchio is exacting his revenge. Allen is out at AT&T. The company is struggling to find a growth strategy. And Nacchio, 48, is getting rich running one of the hottest upstarts in telecom, Qwest Communications International. He joined the company in January, 1997, after meeting Qwest's owner, Philip F. Anschutz, a reclusive dealmaker who had amassed billions in oil and railroads and now was aiming to build a broadband, high-speed communications network.

a minute?" asks ICG's CEO, J. Shelby Bryan. "I wouldn't want to be in that position."

The business that will move most quickly to the converged networks is fax, already a form of data. About 8% of long-distance calls and 40% of international calls from the U.S. are faxes. Losing that business would cost AT&T and its rivals up to \$10 billion a year. "Even if they just lose fax, that could be really problematic for the voice networks," says Mercer's Christner.

Customers are starting to get a taste of what converged networks can do. Ford Motor Co. is using integrated networks to coordinate the efforts of 120 design engineers on five continents. This means that over a single connection, the workers can discuss designs for new cars and share sketches (page 57). (Clothing retailer Burlington Coat Factory fig-

QWEST

Nacchio says the company's success surprises even him

handle all 400 billion minutes of current U.S. telecom traffic.

All this has made Nacchio the poster boy for the "next-generation telcos" and Denver-based Qwest a rising star on Wall Street. Analysts project revenues will soar nearly 50% this year, to almost \$1 billion, but construction costs will cause a loss of some \$50 million after net income of \$14.5 million in 1997. Qwest's stock has nearly tripled, to \$40, since its initial public offering last June. And on Mar. 9, Qwest agreed to acquire LCI International Inc., a company with twice the revenues of Qwest—for \$4.4 billion in stock. "I'm the most surprised guy of anyone at how well we've done," Nacchio says. Sitting on stock options valued at some \$200 million, revenge has seldom been sweeter.

By Steven V. Brull in Los Angeles

Nacchio is off to a galloping start. Virtually all of Qwest's 26,208-km network connecting 125 U.S. cities will be completed by the end of this year. The company has launched 7.5¢-a-minute long-distance service for consumers and is targeting businesses as well.

Nacchio has got plenty of room to take on more customers. Each of Qwest's 48 fibers can handle 500,000 simultaneous telephone conversations—about 12 times more than a traditional phone network is capable of. And even though the company is only using two fibers, Nacchio reckons that's enough to

ures that it will share 30% off its long-distance bill by diverting calls made between its 50 stores to an internal network for data and voice.

PACKETS. And Internet bookseller ABC Bücherdienst is giving its customers better service because of its converged networks. Based in Regensburg, Germany, where labor laws forbid employees to take customers' calls at night on Sundays, the company has found data-voice networks critical. During those hours, people who visit their Web site can click on a button to ask questions of representatives in Florida—where no such restrictive laws exist. "It gives us the ability to answer the calls for nothing," says Michael Gleissner, president of ABC's U.S. operations.

Indeed, the rise of the next-generation telcos stems from a fundamentally new technology. Since Alexander Graham Bell invented the telephone in 1876, the U.S. telephone system has been based in what's called "circuit switching." In its simplest form, this means that an entire telephone circuit is dedicated to a phone call between point A and point B. This is like a driver reserving the whole lane of a highway for a trip from New York to Boston.

The new telcos use a more efficient technology,

called packet switching, which breaks the sounds of a voice call into little packets for transport. The packets from many voice calls can be crammed into a single circuit at the same time, interspersed with data packets. It's similar to many cars traveling in the same lane between New York and Chicago. The cars also are more compact: While standard voice circuits are 64 kilobits wide, the typical packet is only 8 kilobits.

Once the sound of a voice is broken into packets, it looks just like a packet carrying data, fax, or video clip. That results in tremendous efficiencies: The same network that carries voice can carry everything else. And because the kind of packet switching the newcomers are using is IP, the networks can use the same infrastructure that has been built to access the Internet. In most cases, though, the calls don't

go over the Internet because private networks send its faster and more reliably than the clogged public essential for a conversation.

A new telephone companies can also ride the boom of the net and get ever-cheaper, ever-more-efficient equipment such suppliers as Cisco Systems Inc. and 3Com (page already, companies such as Qwest can buy network ment that's 25% to 33% less expensive than traditional according to analysts. Even bigger savings come from additional capacity of the new networks: Analysts say can carry 6 to 10 times the traffic of traditional circuit- ed networks. Overall, Level 3's James Q. Crowe esti- that his network will cost less than 10% of the price of onal lines. "Being an incumbent means having a more lt time than a new entrant," says Crowe.

en so, the telecom giants aren't giving up. The Baby think the technology could jump-start their push into

ng-distance busi- and several, includ- S West Communi- s Group and SBC unications Inc., are the Federal Com- ations Commission ne right to build rged networks. e not going to up and find [our business] is gone," BC Executive Vice- ent for Corporate ing Mike Turner.

BERNED." Most of aby Bells snort at tion that these up- will horn in on core businesses. have to separate pe from the reali- says Ameritech CEO Richard C. aert. "We have mers, real cus- s, paying hundreds lions of dollars to ay. When you look vel 3 and Qwest, any customers do ave?"

e difference is or- of magnitude. But navericks do have vantage: They can paying the Bells s charges. These es that long-dis- companies pay cal players to car- call from a home ice to the long-dis- network, and on its destination. re about 4¢ a ce. Because voice over converged rks are considered these companies ttle if any of these

Four cents a minute adds up. If 13% of the long-distance traffic travels over converged networks in 2002, as consultant Frost & Sullivan projects, the lost access charges would cost the Bells about \$4 billion a year. The Bells are not happy about the prospect.

They argue that it is fundamentally unfair for voice calls over converged networks to avoid access fees, while traditional voice calls pay the freight. "Clearly, it's something we're concerned about," says Lawrence T. Babbio Jr., president of Bell Atlantic Corp.'s network group.

The Bells are hardly alone in their complaints. Legislators whose states use the access charges to subsidize telephone service are bristling. Senator Ted Stevens (R-Alaska) has asked the FCC to review the situation, especially since he feels

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A Real Gusher in the Pipeline



In 1984, Tulsa gas-pipeline operator Williams Cos. was scouting for a way to squeeze a few bucks from abandoned pipelines. It seized on the idea of threading fiber-optic cables through the pipelines and leasing capacity to newcomers then challenging AT&T in long-distance phone services. The idea spawned WilTel Network Services, a business sold to what is now WorldCom Inc., 10 years later for a staggering \$2.5 billion.

For a time, it looked as though the telecom foray would end up a colorful chapter in the history of a \$4.4 billion energy empire. No more. Williams is returning to the communications business—and this time, it will sell wholesale capacity for carrying voice and data. The company plans to double the size of its nationwide network to 22,000 miles by late 1999. It has already won \$1 billion in contracts with U S West Communications Group and Intermedia Communications, a Tampa telecom company.

Still, Tulsa's good ol' boys will face tough competition from newcomers such as Qwest

Communications International. Williams' strategy is to strike alliances with utility giants already re-selling Williams natural gas and electricity, such as Nevada Electric Co.

Williams has another ace up its sleeve: Last year, the company struck a partnership with Northern Telecom Ltd. to sell voice- and data-switching equipment to corporations. The venture, managed by former NorTel exec Garry K. McGuire, already boasts such customers as Bankers Trust New York Corp. "The good news is that demand for bandwidth is growing exponentially," says McGuire. Last year, the communications group saw a loss of \$55 million on \$1.4 billion in revenues, but Prudential Securities Inc.'s M. Carol Coale says it should reach \$85 million in operating profits next year. Call it the Tulsa two-step: You move full circle and wind up back in the same place.

By Gary McWilliams in Houston

WILLIAMS

Bandwidth demand is through the roof, says McGuire

Taking the Net to a Whole Other Level

When WorldCom swallowed MFS Communications for \$14.3 billion in 1996, MFS CEO James Crowe pocketed about \$150 million and nestled in as WorldCom Inc.'s chairman. But presiding over meetings didn't suit the entrepreneurial Crowe. When Walter Scott, chairman of Peter Kiewit Sons Inc., offered Crowe the chance to build a new-age telecom company with \$3 billion in startup capital, he jumped at the chance. "Helping people communicate is what gets me up early in the morning and keeps me up late at night," Crowe says.



Crowe caught Internet fever while at MFS. That's when Microsoft Corp. Chairman William H. Gates III told Kiewit's Scott that the Net would displace switched networks. Once Crowe got the word, he shelled out \$2 billion for Internet pioneer UUNET Technologies Inc., whose network offered higher capacity at less cost than Bell networks. "The light bulb went off for us," recalls Crowe. "We recognized that the Internet wasn't about flashy graphics and

LEVEL 3

Crowe is building a \$9 billion network

Crowe, 48, launched Denver-based Level 3 Communications Inc. in January with an ambitious objective: to triumph in the telecom wars by building a \$9 billion network based on Internet technology that can transmit voice, data, fax, and video. By yearend, Crowe expects to sell data and fax services to big businesses in six U.S. cities. In a decade, he plans to serve more than 60 U.S. cities and others overseas. Industry experts are betting that Crowe's experience at MFS Communications Inc. will help him hit pay dirt again. "The

guy saw the future a while ago," says Randy Storch, CEO of Open Port Technology Inc., a Chicago software company.

While an executive for Kiewit's electrical-utility business in the mid-'80s, Crowe saw his chance when a contractor appealed for money to launch a fiber network. Instead, Crowe persuaded Kiewit to float him \$500 million to start Omaha-based MFS. The company was the first to compete with regional Bells by attracting business clients—many of them Internet service providers.

cool people, it was about the economics of communications."

Level 3 claims it can deliver telecommunications services at less than one-tenth the cost of traditional telephone networks. While analysts agree that its costs are lower, Level 3 lacks two key assets: customers and an established brand name. Still, Level 3 and other rivals have the Bell companies "running like the devil to reinvent themselves," says telecom analyst Jeffrey Kagan. Question is, can they keep up with Crowe?

By Roger O. Crockett in Chicago

AT&T and WorldCom with MCI could try to avoid the fees, too. "You've got the potential for bypass on a massive scale, and it's not too far off," says Mitch Rose, Stevens' chief of staff. "It's coming at us like a freight train." Still, it looks as if the mavericks won't get hit with full access charges anytime soon. There's tremendous public sentiment to leave the Internet untaxed.

So which of the traditional telecom companies are most prepared for the impact of the converged networks? WorldCom Inc. stands head and shoulders above the rest. With the purchase of UUNET Technologies, WorldCom

CEO Bernard J. Ebbers landed the largest carrier of Internet traffic in the world. If WorldCom merges with MCI as planned, it will control by some estimates more than 50% of the Internet backbone—enough that the trustbusters in Washington

So far, WorldCom has kept its voice traffic on traditional networks and is using UUNET to pursue new growth opportunities, such as fax, over IP. But as voice, data, and video converge, WorldCom will have the expertise and the assets to cash in on the boom. "Our vision is to build a phone company that looks more like a Silicon Valley startup," says John

Sidgmore, president and CEO of Fairfax (Va.)-based UUNET GTE Corp., headquartered in Stamford, Conn., is the most aggressive old-line phone company. Last year, it bought BBN Corp., a company that helped create the Internet and has extensive Net assets, and it acquired the rights to one-quarter of the capacity of the high-tech network Qwest building. It's conducting trials with voice and fax over the same network that now carries its data. The company thinks it's inevitable that all the traffic eventually will flow over a converged network. "We're not upgrading—we're putting a brand-new technology from the get-go," says George Conrades, executive vice-president at GTE.

Looking at the economics of the new networks and the potential for new services, analysts say the message to the old phone companies is simple. "You can either cannibalize your circuit-switched network, or you can have someone else do it for you," says James H. Henry, an analyst with Bear, Stearns & Co. That should be a wake-up call.

By Peter Elstrom in New York, with Andy Reinhardt in San Mateo, Calif., Susan Jackson in Stamford, Conn., and

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Special Report TELECOMMUNICATIONS

Charles Schwab

Networks That Do New Tricks

Systems such as Ford's go miles beyond videoconferencing

Last August, designers at Ford Motor Corp.'s studios in Dearborn, Mich., and Merchanick, Germany, were trying to figure out where to put the logo on the new Mercury Cougar. But instead of flying back and forth, they peered into workstations connected to Ford's data-voice-video network and were able to view 3-D images of the car while videoconferencing with each other. Their decision: Put the logo front and center, above the grill. "It's refining details that makes a design that really sings with the customer," says Barry Caldwell, a design supervisor at Ford.

Plain-vanilla videoconferencing is becoming passé at Ford. Integrated voice, video, and data networks such as Ford's are rare, but falling transmission costs and new applications are bringing them into the mainstream. In the next 12 to 18 months, converged networks will be found everywhere, from giant call centers that handle customer phone queries to small businesses using Internet-

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TELECOMMUNICATIONS

based audio-videoconferencing programs.

Ford's network is the gold standard. About 120 designers on five continents sign on daily to Silicon Graphics Inc. workstations linked over high-speed phone lines. Designers can share work without worry over location or time zone.

"AN EXPLOSION." The most obvious savings is the time and money spent on travel. But Ford officials say the ability of designers to collaborate around the globe also boosts quality and efficiency. Still, data network managers at many companies are wary of adding bandwidth-hungry video and data applications that could bog down their intranets. Their opposition is softening, though, as networking gear becomes cheaper and more reliable. "Over the next couple of years, we'll see an explosion in applications that take advantage of [multimedia] networks," says PictureTel Corp. Chief Executive Bruce



Bond. He predicts that up to 60% of **CALDWELL: Re-** PictureTel's 10,000 customers will do at *fining details* least some videoconferencing over multi- *"makes a design* media networks in three years. *that really sings*

Call centers will be among the first to adopt multimedia networks, as they shift to the World Wide Web. In January, Creative Computers Inc. in Torrance, Calif., set up a function at its pemail.com Web site that allows visitors to click on a button and establish a voice connection with a sales agent. The function has boosted sale dramatically, says Creative Computers Sales Director Jonathan Bumba. Agents can explain Web pages on the caller's screen, promote products, and take credit-card information.

Call-center productivity also gets a boost. Integrated networks can identify each incoming call and match it instantly with the caller's account, placing pertinent data on the screen before an agent answers. Calls can even be outsourced to remote agents at home.

Individuals are getting into the act as well. Although voice and video calls over the Web are subject to delays of two seconds or more, programs such as Microsoft Corp.'s NetMeeting are smoothing the process. NetMeeting lets customers run audio or videoconferences while sharing applications. Microsoft estimates there are some 5 million regular users.

And researchers keep developing even more sophisticated applications. A consortium including Ford, Silicon Graphics Sharp Electronics, and others is one of several groups developing "replacement reality." The goal is to go beyond virtual reality with remote technologies that allow more realistic visual, audio, and tactile sensations. Such networks could allow surgeons to guide operations in distant hospitals. That makes designing a logo look like child's play.

By Steven V. Brull in Los Angeles

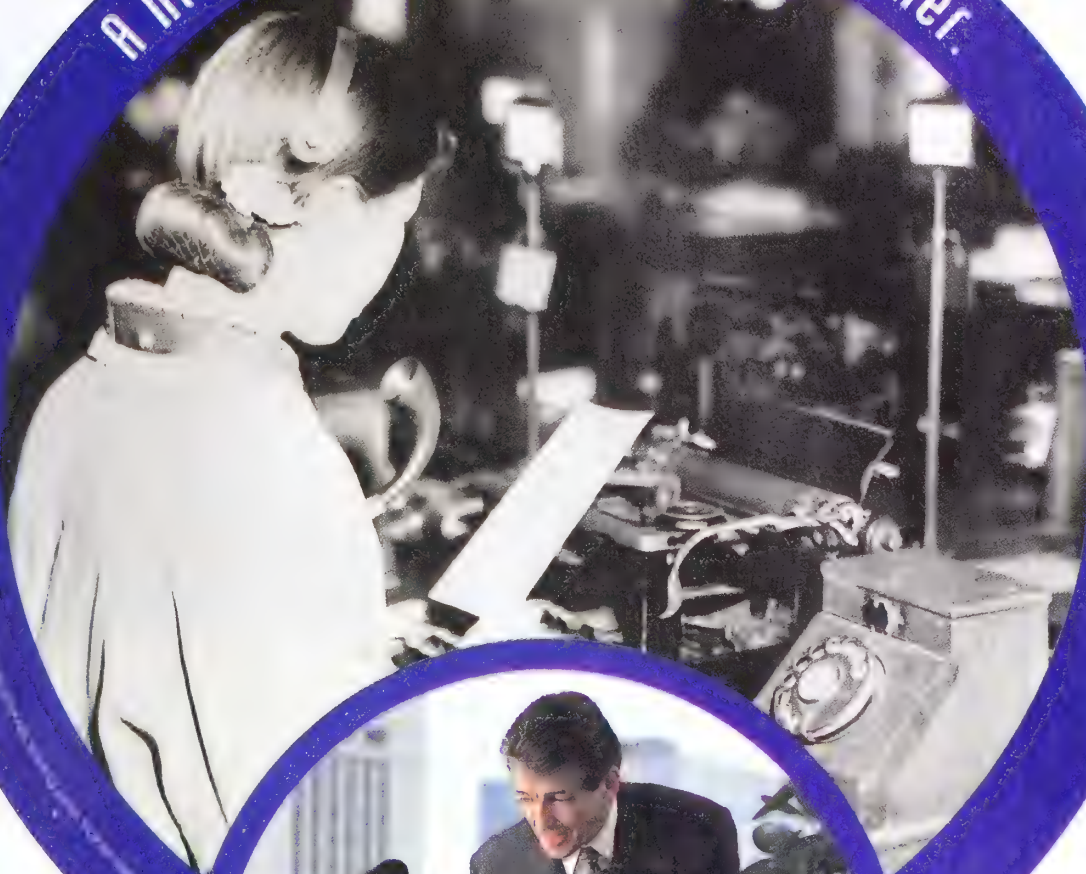
How Users Benefit

COMPANIES Ford, Concentric Network, and a few other companies are integrating voice, data, and video on a single network to collaborate and share documents in real time. With 120 engineers using the technology, Ford estimates it has helped shorten the average car design time from 36 months to 24 months.

CALL CENTERS Call centers have been quick to adopt new technologies that make them more efficient. L. L. Bean takes advantage of integrated networks by allowing visitors at its Web site to click on a button and talk live to a service agent. They can browse the Web and talk to the rep over the same line.

CONSUMERS So far, individuals benefit from the new networks primarily through inexpensive phone rates, such as the 7.5¢-a-minute offered by Qwest. A key reason: The new networks avoid access charges that average about 4¢ a minute. Individuals will start seeing more advantages of integration soon.

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Special Report

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'The Bell-heads vs. the Net-heads'

Converged networks are the next gold rush. Who will lead the charge to build them?

John A. Roth is serious about the Internet. So serious that the chief executive of telecommunications equipment giant Northern Telecom Ltd. sent a memo to his 73,000 employees last Dec. 3 hinting that their jobs could be on the line if they didn't get Net-savvy—fast. True, Nortel was already working to bridge the gap between the rival worlds of telephones and data networks. But, he said, "it's critical that we accelerate."

That's a rallying cry heard throughout the \$175 billion telecom equipment industry. Titans such as Lucent Technologies, Siemens, and Alcatel have reason to worry: Although the Net is used today mostly for sending data, it's quickly becoming a vehi-

The Interlopers

REVENUES IN BILLIONS

CISCO SYSTEMS	\$6.4
3COM CORP.	\$5.6
BAY NETWORKS	\$2.1
NEWBRIDGE NETWORKS	\$1.4
ASCEND COMMUNICATIONS	\$1.2
VOCALTEC	\$0.157

CISCO'S

CHAMBERS: *His company "is in a position to lead this industry"*

cle for voice calls. Customers love the combo: Shifting voice traffic onto data networks saves them big bucks on long-distance bills. By 2002, predicts researcher Frost & Sullivan, some 13% of the world's phone calls could be carried over Internet-type networks, instead of through old-style voice switches.

Sensing the threat, phone equipment makers want a piece of the market for voice-over-Internet gear. It won't come easy: Fast-moving Cisco Systems and 3Com Corp., which dominate the data networking business, are gunning for the same big game. "Call it the Bell-heads vs. the Net-heads," says Jayshree Ullal, marketing vice-president of Cisco's enterprise unit. By 2002, sales of such gear could hit \$13 billion, up from \$680 million this year, according to researcher Killen & Associates. If data networking firms grab this market, their growth rates could climb by 10 percentage points, predicts 3Com CEO Eric A. Benhamou. Says analyst Paul Johnson of BancAmerica Robertson Stephens: "This will be a battle of the giants."

NOW HIRING. It's too early to call a winner, but analysts give the edge to telco equipment makers. Their sheer size—Lucent has three times Cisco's revenues—and long relationships with phone customers give them an inside track. "Lucent has something Cisco lacks: credibility in the telco market," says analyst Amar Senan of Volpe Brown Whelan & Co. Even Cisco CEO John T. Chambers concedes that he and his rivals must make data gear as reliable as voice—task he's confident he can accomplish. "Cisco is in a position to lead this industry," he says.

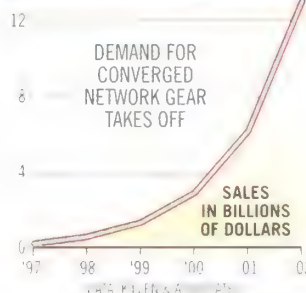
The Net-heads are certainly trying. On Feb. 4, Bay Networks Inc. sank \$38 million into startup Net Speak Corp., which makes a telephone gateway for connecting voice switches to the Internet. Ascend Communications Inc. is set to roll out its voice products on Mar. 30, while "Cisco is hiring telecom people like mad," says John Coons, an analyst for researcher Dataquest Inc. Data companies argue that they understand networking better than the voice crowd. "It'll be a long, slow march for them to get into this world," crows Bay Networks Executive Vice-President Steve G. Pearse.

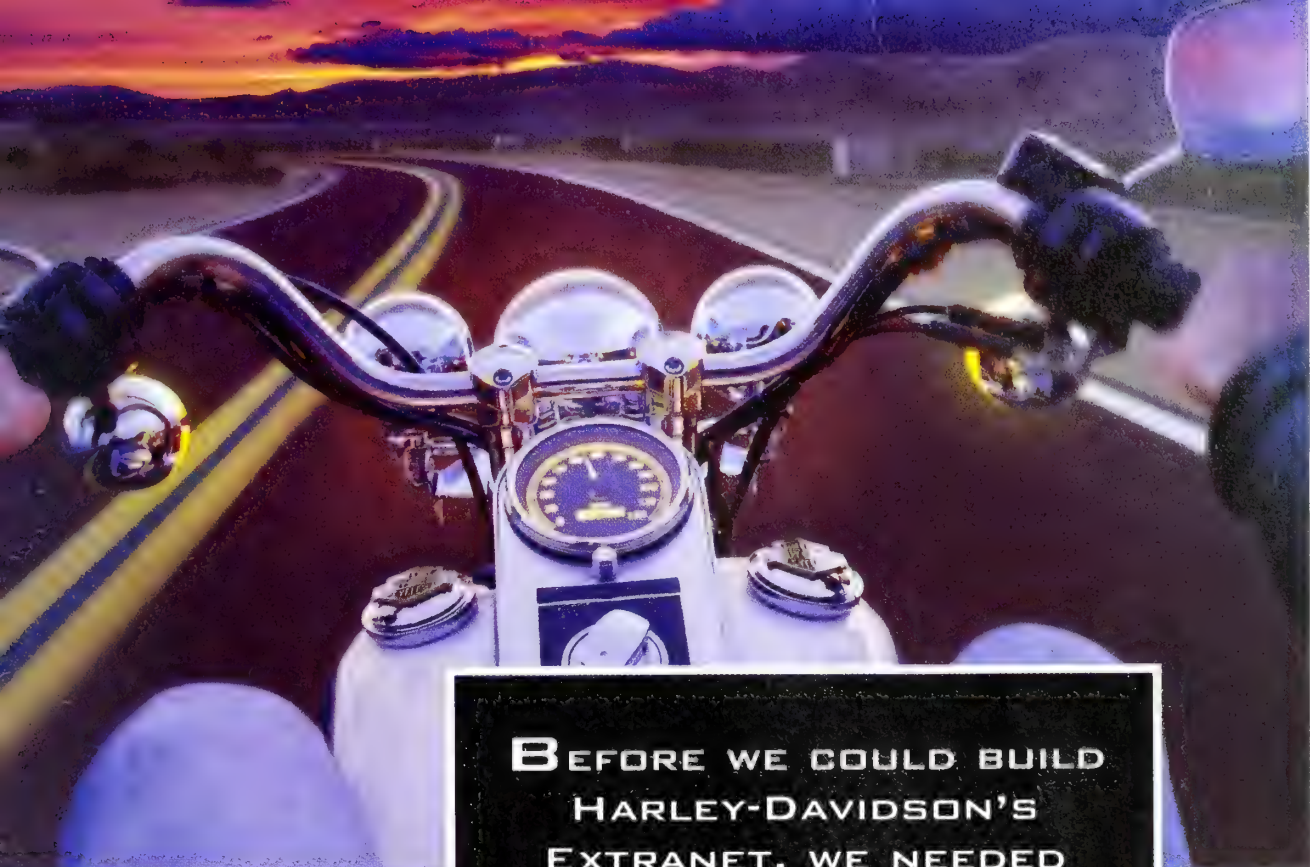
Maybe not. Telecom equipment companies are rushing to add data capabilities. On Mar. 18, Nortel spent \$290 million to buy Aptis Communications, a maker of speedy devices that connect users to the Net. And Lucent, AT&T's former equipment business, has devoured a string of small networking firms, including Livingston Enterprises Inc. "We are going after the data business," vows William T. O'Shea, president of Lucent's business communications systems unit.

Startup voice-over-Internet phone companies, such as ICC Communications Inc., certainly aren't dismissing the old guard. ICC's network uses a mix of Cisco and Lucent gear. That impresses analyst Senan, who says the deciding factor in grabbing market share will be whether companies operate "in Internet time or telco time." You don't need to tell Nortel's Roth. He's got his troops marching to a cyberbeat.

By Andy Reinhardt in San Jose, Calif.

Look Who's Talking





**BEFORE WE COULD BUILD
HARLEY-DAVIDSON'S
EXTRANET, WE NEEDED
TO GET A BETTER FEEL FOR
THEIR BUSINESS.**

*How do you cut a
warranty claims process from
three weeks to three days?
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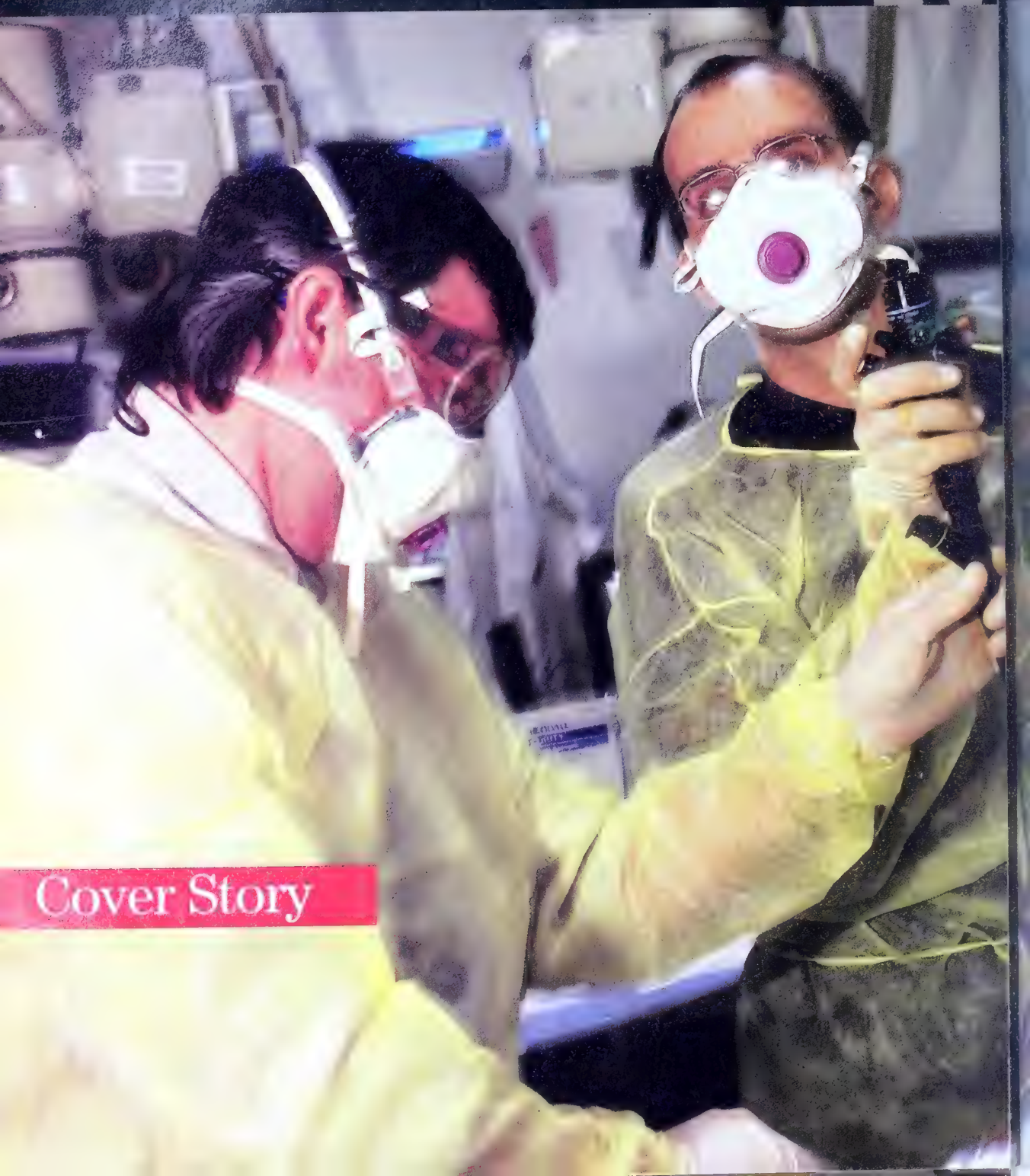
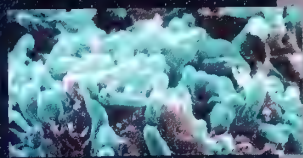


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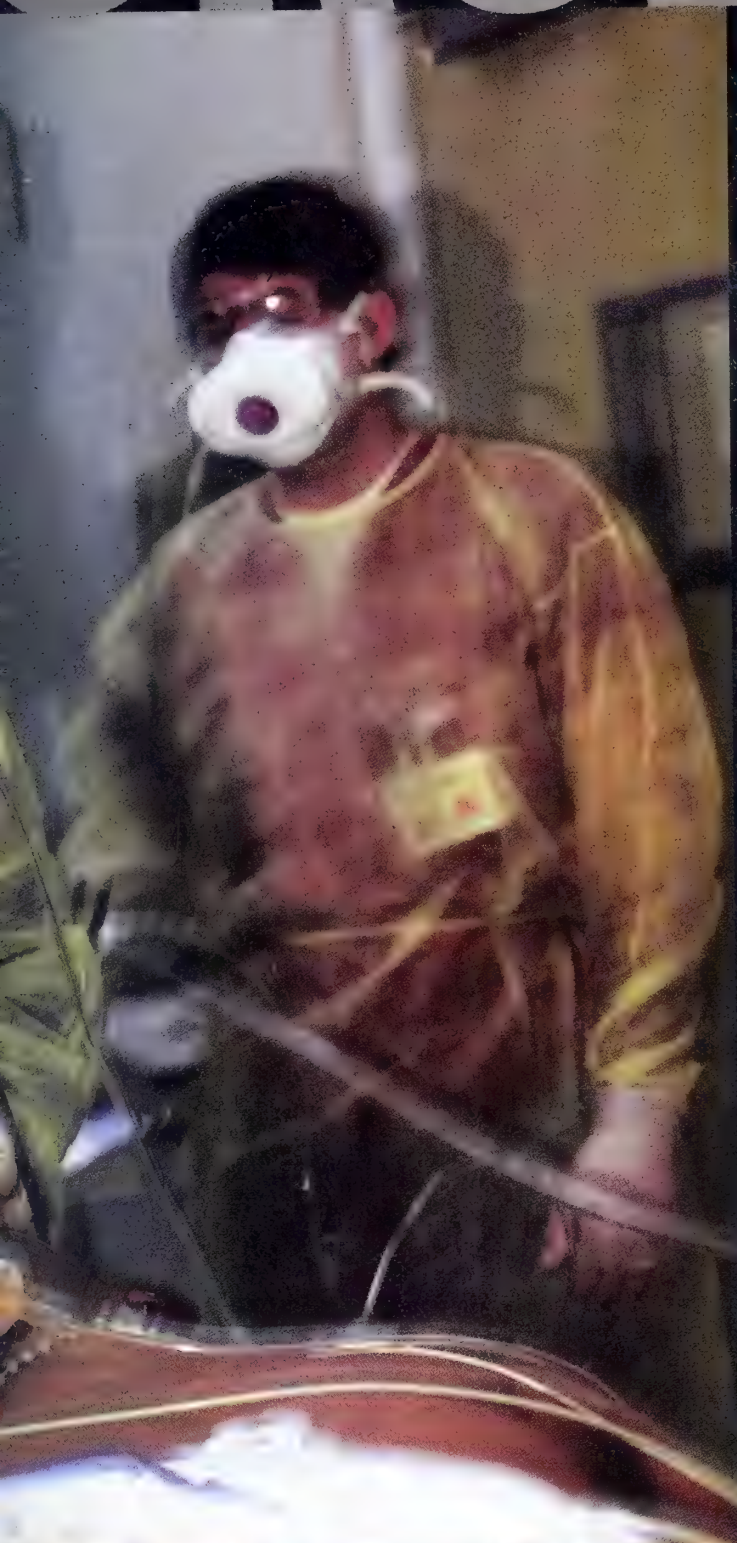
Microsoft®

WAR *against* *the*



Cover Story

GROBES



As deaths from infections surge, medicine is racing to regain control over superbugs

One of the greatest triumphs of human ingenuity has been our progress against infectious disease. Today, we have only the mute testimony of millions of gravestones to remind us of the lives tragically cut short by scarlet fever, polio, smallpox, or rampant infections of childbirth. But these mighty conquests are of small comfort to Christy and Chad Gimmestad of Evans, Colo. Their 16-month-old daughter, Anna Grace, died in late 1996 during a worrisome outbreak of *E. coli* 0157:H7, a vicious microbe unknown until 1980. *E. coli*'s rampage continues: It sickened 16 people in Colorado last year.

Nor is the miracle of penicillin and other antibiotics much consolation to the families of the 33 people who have died of rampaging

ON THE DEFENSIVE

Doctors and staff at Bellevue Hospital in New York take precautions against airborne bacteria during diagnostic procedures to detect tuberculosis

PHOTOGRAPH BY STEVE RUBIN; INSET BY OLIVER WECKES/PHOTO RESEARCHERS

The Warriors

are searching for ways to cripple deadly viruses and solve the mysteries of lethal bacteria



DR. DAVID SHLAES

Drug companies "forgot a few minor things. Namely, resistance," says the Wyeth-Ayerst vice-president

DR. LISA DEVER

In the front lines treating infected patients at the East Orange (N.J.) veterans' medical center



strep A infections since December in Texas. And our successes treating the terrible lung disease tuberculosis may not have much meaning for California teenager Debi French. In 1993, French came down with a TB infection potent enough to fight off even today's miracle drugs. Only after a two-year struggle—and the surgical removal of nearly half of her right lung—did the high-schooler come out on top in this battle of humanity vs. the microbes. On Mar. 18, the World Health Organization warned that TB could infect 1 billion more people in the next 20 years.

The sobering truth is that while we have won many such battles, the war is still raging. But now, researchers are rearming. After a decade of relative in-

Cover Story

action, pharmaceutical companies have stepped up their efforts to find new drugs, vaccines, and other treatments to knock back the microbial hordes. "We're seeing the tide shift dramatically," says James F. Young, senior vice-president of research and development at MedImmune Inc. in Gaithersburg, Md. "Industry is jumping into antibiotics and vaccine development with everything we've got."

GRUESOME DEATHS. That may be a bit overstated. Research on infectious diseases still lags efforts on, say, heart disease. But any progress is urgently needed. Scarcely a week goes by without a report of some dire and growing threat. Mysterious hantaviruses are causing gruesome deaths in the West. Potent new forms of TB are emerging in Tennessee and Kentucky. Staph germs that don't respond to the most commonly used antibiotics are spreading from



HY ROLPH AND
ES MERSON ▶

Success of HIV
tests bodes well
for antiviral efforts,
Pfizer's Merson

SELL

ly's infectious
research, she
renewed effort
against microbes



go hospitals to the surrounding
community.

In fact, more than 30 dangerous new
agents have been discovered
in the past two decades. The death rate
in the U.S. from infections jumped
by 58% between 1980 and 1992,
partly because of AIDS and an aging
population, which is more susceptible
to germs. Researchers estimate that
hospital-acquired infections alone are re-
sponsible for a staggering \$4.5 billion
in annual U.S. health-care costs.

The situation is far grimmer else-
where. With malaria, TB, and dengue
fever on the rise, microbes are now
causing one-third of the world's 50 mil-
lion deaths each year. "We are see-
ing a global resurgence of infectious dis-
ease," U.S. Surgeon General David
Satcher warned Congress on Mar. 3.

KEY POINT. Experts say humanity
is at a crucial turning point in the
century-old war against microbes. One
factor is the explosion in world popula-
tion. Another is air travel—the dead-
ly infectious diseases are only a plane
ride away from New York, London, or
Sydney.

Most ominously, though, microbes
have been hard at work in a deadly
game of mutating to create potent new de-
sires far beyond the reach of many
existing treatments. "We have never
been more vulnerable," says microbiolo-
gist and Nobel laureate Joshua Leder-
berg. "When I go through all the adap-
tations [made by] the microbial world to
survive at a living at our expense, I some-
times wonder how we're still here."

But microbes aren't the planet's only
threat—species—and humanity is fighting
back. One part of the solution is to beef
up global surveillance and respond
quickly to diseases, squelching outbreaks
before they explode into epidemics. A

second is boosting prevention (page 112).
On Mar. 19, for instance, Agriculture
Secretary Daniel R. Glickman unveiled a
plan for dousing chickens with harm-
less bacteria so the "good" bugs will
prevent disease-causing salmonella from
contaminating poultry flocks.

The final piece of the puzzle is the de-
velopment of new drugs and vaccines.
Drugmakers around the globe sharply
curtailed efforts to develop new antibi-
otics in the 1980s, deciding the market
was crowded and satisfied. "They forgot
a few minor things," says Dr. David M.
Shlaes, vice-president of infectious dis-
ease research at American Home Pro-
ducts' Wyeth-Ayerst Research unit.
"Namely, resistance." Now top re-
searchers at Wyeth-Ayerst, Pfizer, Ab-



▲ **DR. FRANCIS TALLY**

*At Cubist Pharmaceuticals
in Cambridge, Mass., he
uses new genomic weapons*

bott Laboratories, Merck, SmithKline
Beecham, Glaxo Wellcome, Schering-
Plough, and a host of biotech compa-
nies are launching an assault against
infectious disease.

The counterattack is by no means
comprehensive—efforts directed against
the world's biggest killers, such as TB
and malaria, are disappointingly small.
But there is hope for a slew of new
and better drugs and vaccines against
everything from pneumonia and staph
to flu and hepatitis. According to the Phar-
maceutical Research & Manufacturers
of America, 125 drugs aimed at infec-
tious disease were in the pipeline in
1996, up from just 79 two years earlier.

Fueling the hope for better treat-
ments are rapid advances in technology

IN THE HEADLINES: *The Revenge of the Microbes*



PREVENTION: *Inoculating kids in Rhode Island*

- Out of 134 total cases, 33 Texans die from **STREP A** between Dec. 1 and Mar. 20
- **HEPATITIS A** strikes 147 residents of

Spokane County, Wash., so far this year

- **SYPHILIS** cases in Baltimore have more than tripled since 1993, and

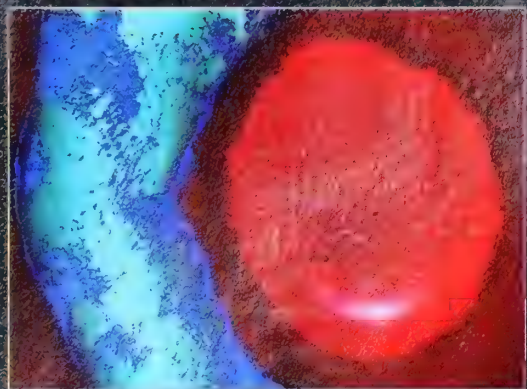
other sexually trans-
mitted diseases are
on the rise there

- The World Health Organization warns on Mar. 18 that a **TUBERCULOSIS** epidemic could infect more than 1 billion people, killing 70 million of them, in the next 20 years

- Hamburger meat contaminated with **E. COLI O157:H7** sickens 16 people in Colorado in June last year

WE HAVE MET THE ENEMY...

Researchers around the globe are scrambling to develop new drugs to combat these increasingly dangerous organisms:



1) STREPTOCOCCI (bacteria)

A leading cause of illness and death among both children and the elderly is *Streptococcus pneumoniae*. Increasing numbers of cases in the U.S. are resistant to penicillin, and some are resistant to other classes of antibiotics as well.

that speed up drug discovery. Robotics and high-speed equipment allow researchers to test thousands of compounds against a disease target in one day. And the gene-sleuthing revolution has made it possible to finally understand what makes bugs tick—and how to attack them at their most vulnerable points. "We are stripping these beasts bare, exposing their genetic secrets, and turning that information against them," says Alan R. Proctor, an executive director of research at Pfizer Inc.

Advances are already saving lives.

ria," says Rhône's Gary T. Shearman, who oversees drug development. "But we need all the weapons we can get."

The search for new weapons has led some companies to reconsider candidates once rejected. At Schering-Plough Corp., an antibacterial chemical called Ziracin had been kicking around for more than a decade. But Schering set it aside because it proved too toxic in many patients. Remembering how potent the drug was, Schering began to give it another look three years ago. Tests showed that a new, less toxic intravenous form wiped out more than 5,000 different strains of bugs. Now, company scientists are racing to do larger tests of its safety and effectiveness in people. Dr. Lisa Dever, head of the infectious diseases clinic at the East Orange (N.J.) Veterans Affairs Medical Center, has done some tests of Ziracin and describes the results so far as "nothing short of amazing."

Other companies are employing clever strategies to outwit drug-resistant bacteria, thus prolonging the usefulness of existing weapons. Killer microbes such as staph have evolved the ability to dice up penicillin and pump out tetracycline before either antibiotic has a chance to

work. But what if doctors could add another drug that attacks the defense system? That would enable the original antibiotic to still fight the infection. Microcide Pharmaceuticals Inc., in Mountain View, Calif., is developing a compound with Daiichi Pharmaceutica U.K. Ltd. to do just that. Their drug cripples the antibiotic pump used by the bug, *Pseudomonas aeruginosa*, which causes lung infections. Wyeth-Ayerst is working on a new form of tetracycline that can get around the defense mechanisms of bugs like enterococci.

But shoring up old drugs may only buy a little time. What's urgently needed are new classes of compounds that attack bugs in new ways. First on the scene are likely to be antibiotics called oxazolidinones. These were discovered by DuPont Co. in 1987 the old-fashioned way—researchers dumped chemical onto bacteria and waited to see if the bugs died. Scientists subsequently learned that the oxazolidinones kill bacteria in a way that's completely different from any existing drug. These compounds seem to gum up the work of the cell's protein-making factories at a different location than do other drugs. Researchers at Pharmacia & Upjohn Inc., which has such a drug in final tests, hope that because the bacteria haven't seen this avenue of attack before, they will be slow to develop a defense.

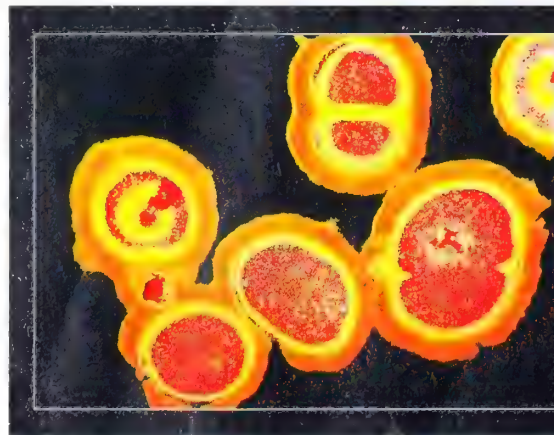
The company plans to file a new drug application on the oxazolidinone antibiotic as early as 1999. Bayer AG Group is also working on such a drug, and Dr. Stefan Wohlfeil, head of anti-infective research at Bayer, says he's keeping his fingers crossed that unexpected problems don't crop up. "If anything happens to this class," he warns, "there isn't much on the near horizon."

The more distant horizon, however, is bursting with promise—thanks to a revolution in molecular biology. Researchers have learned to decode the entire DNA sequences of lethal microbes. That makes it possible for scientists such as Dr. Francis P. Tally at Cubis

Cover Story

On a spring day in 1993, Dr. James J. Rahal at The New York Hospital Medical Center of Queens was in a panic. His patient, a 46-year-old woman, had developed a life-threatening infection in a major artery after vascular surgery. Doctors tried six different antibiotics. None worked—not even Vancomycin, usually the superdrug of last resort. "Chances are that she would have died," says Rahal. Fortunately, a colleague had read about an experimental drug, Synercid, being developed by Rhône-Poulenc Rorer Inc. in Vitry-sur-Seine, France. Rahal got on the phone: Could Rhône send him the drug immediately?

JUST IN TIME. In France, Rhône scientist François Bompard swung into action, wresting permission from the U.S. Food & Drug Administration to ship the drug to New York. Rahal rushed to inject it into the patient—just in time. Synercid completely wiped out the *Enterococcus faecium* in her system. Since then, the drug has been given to more than 3,000 patients on an emergency basis, and an FDA committee recently recommended that the drug be approved quickly. "This is one victory in the war against bacte-



2) STAPHYLOCOCCI (bacteria)

One kind, *Staphylococcus aureus*, is commonly acquired in hospitals. A few recent cases of the bug developing resistance to Vancomycin, which is the antibiotic of last resort, set off alarms in the medical community.

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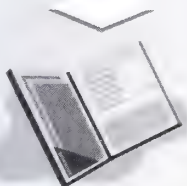
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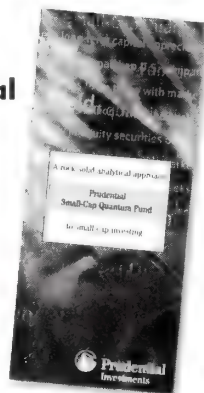
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Pharmaceuticals Inc. to uncover the biological pathways that pathogens need to survive. "Bacteria are no longer black boxes," says J. Craig Venter, president of the Institute for Genomic Research (TIGR), the Rockville (Md.) laboratory that has led the way in microbial gene sequencing. "It's like going into a dark room and turning on the light switch."

That light, however, can be blinding. The first microbe whose entire genetic sequence was decoded by TIGR researchers was *Haemophilus influenzae*,

Cover Story

a cause of ear infections and meningitis. It contains 1,740 genes; others have even more. It's a huge amount of information—the trick is figuring out which pieces are important. "It's like going into a Russian library when you don't speak Russian," says Kelvin Cooper, a director of medicinal chemistry at Pfizer Inc. In labs of both big drugmakers and small biotech operators, PhDs hover over computers, crunching the mounds of data generated by the genetic sleuthing. Comparing well-un-

derstood gene sequences from other organisms to those of the bugs, they look for similarities. That gives a clue to what certain genes do—and where the microbe's defenses are weakest. **DISARMING.** Consider the tale of tRNA synthetase, one in a long list of possible drug targets. It is an enzyme used to shuttle around amino acids, the building blocks of proteins. There is a different tRNA synthetase for each of the 19 amino acids. Prevent any one of them from doing its job, and wham!—the whole cell shuts down.

Back in the late 1970s, SmithKline

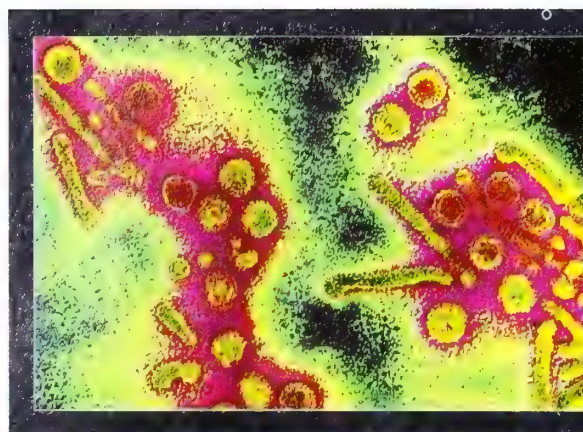
scientists figured out that an existing drug, Bactroban, kills *Staphylococcus aureus* bacteria by gumming up one of those enzymes. In 1994, genetic sleuthing helped the company identify the other 18 tRNA synthetases in staph aureus and 19 previously unknown genes and enzymes in *Streptococcus pneumoniae*. "All of a sudden, we had 19 new targets for drugs," marvels Martin Rosenberg, head of anti-infectives research at SmithKline. The company has launched a major screening pro-

gram to find drugs capable of blocking all the new targets.

A completely different tack is to search out microbial genes responsible for disease. When they're just drifting through the air, lethal bugs activate only the genes they need to live. But when they find a juicy human to infect, they turn on genes that make toxins, ward off the immune system, and otherwise wreak havoc. Some of Microcide's scientists are searching for these "virulence" genes—and for drugs to block them. "We are looking for ways to disarm the bacterium rather than

kill it," says CEO James E. Rurka.

Researchers are also looking for new drugs to attack viruses. There, the hard-won lessons of HIV may pay off against scourges such as hepatitis B and C, which, combined, infect 360 million people worldwide. Drug companies already know that by blocking HIV's reverse transcriptase enzyme they can stop the virus from copying itself, and they are going after the same target in hepatitis. Glaxo Wellcome PLC is expected to launch its AIDS drug lamivudine for he-



3) HEPATITIS B AND C (viruses)

These infect 360 million people worldwide. While a vaccine exists for hepatitis B, resistance to treatment often develops in those already infected. No widely effective antivirals exist for hepatitis C.

The battle against HIV has taught some critical lessons: "Hit hard, and hit early," says one drug company executive

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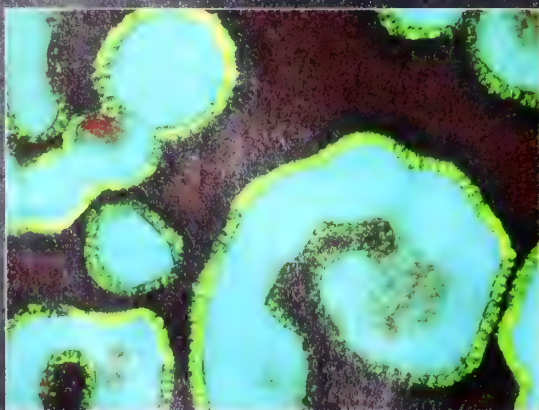
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patitis next year, and Bristol-Myers Squibb Co. is beginning the final phase of clinical trials on a drug called lobucavir for use against hepatitis B and cytomegalovirus, a common infection striking HIV patients. James R. Merson, who, along with Timothy R. Rolph, is leading Pfizer's charge against viruses, notes: "The success we've had with HIV bodes well for what we should be able to do against other viruses."

Perhaps the best way to conquer viruses, however, is by preventing infection with vaccines. Companies are still more than a decade away from an AIDS vaccine. But for other diseases, the new genetic information is leading to rapid progress. The old-fashioned way of making a vaccine is to grow a virus and then kill or weaken it. When administered, the dead or impotent virus prods the immune system into making protective antibodies. But the approach can be too slow or costly to counter a sudden epidemic. Protein Sciences Corp., based in Meriden, Conn., is using a more sophisticated approach. Its researchers have isolated an influenza virus protein that plays a key role in helping the virus attach to other cells. Injecting the protein into the body prompts the formation of antibodies that keep the virus from at-



4) INFLUENZA (virus)

Vaccines exist for the flu, but many people do not get vaccinated. There are few good treatments available once someone is infected. Identifying the flu virus is also difficult because of the lack of easy-to-use diagnostic tools.

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A P P L I C A T I O N S

tacking cells. Tests at the Agricultural Research Service lab in Athens, Ga., show that the vaccine can protect chickens against the avian flu strain that paralyzed Hong Kong last year.

It will be years before many of these research efforts produce vaccines and drugs in the never-ending war on microbes. It doesn't help that the re-

Cover Story

search effort in industry, while impressive, falls far short of what most public-health experts would like. The problem is economics. The antibiotics and vaccines developed in the 1950s, '60s, and '70s are so cheap and still so effective in most cases that the markets for new treatments are uncertain.

Moreover, there are troubling holes in drugmakers' counterattack. The developing world can't afford most drugs. That means the greatest scourges are largely ignored by industry. One of these, malaria, infects 500 million people and cripples economies from sub-Saharan Africa to Southeast Asia. Another, TB, kills 3 million people per year.

Some progress has been made against tuberculosis. An improved anti-TB drug from Hoechst Marion Roussel Inc. is being reviewed by the FDA. And Glaxo Wellcome has signed an agreement with researchers at Albert Einstein College of Medicine to develop a drug that is effective against TB strains resistant to other antibiotics. Still, TB, like malaria, attracts fewer resources than other infectious diseases. And it's not hard to figure out why, says Gail H. Cassell,

who oversees Eli Lilly & Co.'s infectious disease research: "There's been the least effort to develop new anti-infectives [against these diseases] because of the inability of the population in the most affected areas to pay."

That's just one reason the war with microbes may never be fully won. Companies and nations need to launch—and maintain—effective campaigns not only against strep and flu but also against the scourges that ravage far too many of the world's people. Only then would we have a chance of relegating these killers to the pages of our history books.

By Amy Barrett in Philadelphia and John Carey in Washington, with Rick Melcher in Chicago, Larry Armstrong in Mountain View, Calif., and Julie Flynn in London

SOMETIMES THE ANSWERS ARE SIMPLE

The prospect of a microbial resurgence is chilling not only in terms of human suffering but in its cost to the economy. As late as 1938, one study estimated malaria was robbing the South of one-third of its industrial output. Today, an epidemic of staphylococcus resistant to Vancomycin—often considered the antibiotic of last resort—would disrupt the most common medical practices. "Surgery as we know it would have to change," warns Barry R. Bloom, an infectious disease expert at Albert Einstein College of Medicine.

Public-health experts already know how to prevent such disasters. The first step is global vigilance. It's far better to snuff out or prevent a small outbreak than fight an epidemic. With last year's Hong Kong flu, once the avian strain was spotted in humans, microbe hunters around the world speedily unlocked its genetic secrets. Local officials ordered millions of chickens slaughtered. A potential nightmare was averted—demonstrating the power of a swift response.

But the public-health defenses are not impregnable. The Centers for Disease Control, says the Institute of Medicine's Dr. Polly F. Harrison, "wouldn't be able to simultaneously deal with cholera in India, ebola in

Africa, and avian flu in Hong Kong."

And prevention efforts are riddled with holes. Controversial needle-exchange programs, which slow the spread of HIV, aren't being funded. Syphilis cases in Baltimore have tripled since 1993, in part because agencies don't have the resources to track down and treat patients' sexual contacts. Then there's sloppy hygiene.



HONG KONG SCARE

After an outbreak of avian flu killed six, quick action prevented what could have been a pandemic

In the Mar. 12 issue of the *New England Journal of Medicine*, researchers reported the cause of a potentially fatal yeast infection striking newborns at a Lebanon (N. H.) hospital: workers who didn't wash their hands after playing with their dogs.

Medical authorities must also ad-

dress the misuse of drugs. In 1954, the U. S. produced 2 million pounds of antibiotics; today the total is more than 50 million. Almost half is used to boost livestock growth—a practice that horrifies many disease experts. "It is the perfect formula for selecting increasing numbers of antibiotic-resistant bacteria," says Tufts University microbiologist Stuart B. Levy.

Doctors and patients are at fault, too. Levy figures half of all antibiotic prescriptions are unnecessary: "It's a major public-health crisis." Antibiotics are powerless against viruses yet are given routinely to patients with viral infections—spurring resistance. Plus, many patients don't take the full antibiotic course, also spurring resistance. "If we released 10 new life-saving antibiotics tomorrow, in 10 years we'd have resistance problems with them, too, unless we change our practices," says Dr. John D. Siegfried of Pharmaceutical Research & Manufacturers of America.

The CDC has kicked off a campaign to convince doctors and patients to rein in antibiotic prescriptions and use drugs properly. So we know how to beat back the microbial hordes. But do we have the will?

By John Carey in Washington, with Amy Barrett in Philadelphia

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MUTUAL FUNDS

THIS PARTY IS STILL JUMPING

Fund returns are impressive, and the money is pouring in at a torrid pace

After a torrid three years in which the average U.S. diversified mutual fund doubled its shareholders' investment, you would think the stock market and the funds would take a breather this year. Think again. After a rocky beginning, the stock market is once again zooming ahead at warp speed.

And just as in each of the past four

years, the Standard & Poor's 500-stock index, up 13.17% for the quarter (through Mar. 23), is trouncing the average mutual-fund manager. Still, the average equity fund has posted 10% total returns since New Year's (appreciation plus reinvested dividends and capital gains). U.S. diversified funds are up nearly 11% for the first quarter. So who's going to complain?

Certainly not fund investors. They're voting with their dollars—to the tune of \$1 billion a day in recent weeks, says Charles Biderman of Trim Tabs Financial Services, a Santa Rosa (Calif.) firm that tracks mutual-fund inflows. At that rate, he says, the funds will take in \$2 billion this month and some \$54 billion for the quarter. Index funds—low-cost portfolios designed to track a market index rather than beat it—command around 10% of the inflows.

CLOSED WINDOWS. The overwhelming majority of fund buyers still put the money in the hands of stock-pickers. But they're favoring big funds that invest in blue chips, which is another reason small-cap and mid-cap funds continue to lag. Indeed, on Mar. 19, fund giant Fidelity Investments announced it would close three behemoths to new investors—including the \$40.9 billion Fidelity Growth & Income and \$32.2 billion Fidelity Contrafund—lest the portfolio managers get swamped by the torrents of cash. Fidelity did the same to its Fidelity Magellan Fund last fall—and its performance vs. the S&P 500 has improved (table).

Cash is coming back to bond funds as well, and 1998's first quarter should show the strongest inflows in four years. Still, the money is going mainly into higher-return funds, such as high-yield bond funds, leaving the meat-and-potatoes government and municipal funds all but ignored. Taxable bond funds earned an average 1.76% return so far this year, tax-free funds just 0.76%. The quarter's best-performing bond fund, Phoenix Emerging Markets Bond A, up 9.65% (table, page 116).

Fund investors are also sending their dollars abroad once again. Emboldened by their surprise success at home—the U.S. market has already gained far more than most soothsayers had fore-

The Best Performers

Telecom and European funds lead the pack

TOTAL RETURN*		TOTAL RETURN*	
MATTHEWS KOREA I	62.50%	PHOENIX INTERNATIONAL A	20.80%
ULTRAOTC PROFUND INV.	38.76	TEXAS CAPITAL VALUE & GROWTH	20.71
MONTGOMERY GLOBAL COMMUNICATIONS R	36.42	MARSICO FOCUS	20.60
TOCQUEVILLE INTERNATIONAL VALUE	29.76	FIDELITY NORDIC	20.60
FIDELITY SELECT TELECOMMUNICATIONS	27.21	ALLIANCE NEW EUROPE A	20.57
ULTRABULL PROFUND INV.	25.17	FIDELITY EUROPE CAPITAL APPRECIATION	20.44
BARTLETT EUROPE A	23.93	IVY GLOBAL A	19.95
LORD ABBETT INTERNATIONAL A	23.87	MONTGOMERY INTERNATIONAL GROWTH R	19.92
TRANSAMERICA PREMIER AGGRESSIVE GRTH. INV.	23.73	CONCERT INVESTMENT INTL. EQUITY A	19.88
SMITH BARNEY EUROPEAN B	23.72	BJB INTERNATIONAL EQUITY A	19.75
INVESCO WORLDWIDE COMMUNICATIONS	23.47	FIRST EAGLE INTERNATIONAL Y	19.74
PIONEER EUROPE A	22.87	TRANSAMERICA PREMIER SMALL CO. INV.	19.70
FLAG INVESTORS TELEPHONE INCOME A	22.82	MONTGOMERY INTERNATIONAL SMALL CAP R	19.64
SCUDDER GREATER EUROPE GROWTH	22.74	T. ROWE PRICE MEDIA & TELECOM.	19.60
GT GLOBAL EUROPE GROWTH A	22.63	PBHG LARGE CAP 20	19.51
INVESCO EUROPEAN	22.54	RYDEX OTC	19.36
MONTGOMERY GLOBAL OPPORTUNITIES R	22.42	INVESCO EUROPEAN SMALL COMPANY	19.35
OAK HALL EQUITY	22.41	VANGUARD INTL. EQUITY INDEX EUROPEAN	19.27
FEDERATED INTERNATIONAL EQUITY A	22.24	FEDERATED INTERNATIONAL SMALL CO. B	19.26
WEITZ HICKORY	21.73	ICON SOUTH EUROPE REGION	19.16
PRUDENTIAL EUROPE GROWTH B	21.23	AMERICAN CENT-20TH CENT INTL. DISC. INV.	19.14
WADDELL & REED GROWTH B	21.21	FTI INTERNATIONAL EQUITY	19.10
NICHOLAS-APPELATE INTL. SMALL CAP GR. A	21.11	RYDEX NOVA	19.05
WADDELL & REED INTERNATIONAL GROWTH B	21.00	DEAN WITTER GLOBAL UTILITIES B	19.01
ST GLOBAL TELECOMMUNICATIONS A	20.85	DEAN WITTER EUROPEAN GROWTH B	19.00

*Appreciation plus reinvestment of dividends and capital gains before taxes, Jan. 1 through Mar. 23, 1998

DATA: MORNINGSTAR INC.

Cash is coming back to bond funds as well, and 1998's f

for the entire year just a few months ago—they are confident enough to go shopping in the bat-markets. Look at Matthews' I Fund, which between rising prices and a depreciating yen lost 65% of its net asset value in 1997. It's 1998's best performer, up 62.5% (table). And its assets under management are up 10-fold this year, as bargain hunters pour in. At \$108 million, it is far larger now than it was before the crisis.

Still, the pain of last year's Asian market meltdown has not entirely faded away. Biderman estimates that at the end of the quarter, cash flows to international funds will be \$4 billion, down from \$14 billion in the first quarter of 1997.

Cash flows follow performance, and if international funds continue to make gains, the cash will follow. Foreign investors, which can put their money anywhere except the U.S., are up a remarkable average 13.93% so far this year, according to Morningstar Inc., which prepares the data for BUSINESS WEEK (table, page 116). Even with the Asian news Korea rebound, the Asian funds on average are making only modest gains. The average Pacific/Asia funds exclude Japan are up 5.26% for the year, and those including Japan just 1.87%. Japanese funds themselves are up 1.87%.

BOOST. The Asian economies, says manager G. Paul Matthews, who manages three other Asian funds in addition to the Korea portfolio, are in varying stages of recovery. The big picture in Asia is encouraging, he says: "We have an agreement with the International Monetary Fund, a new president, some stabilization. From here, it's a company-restructuring story." He's encouraged by the improvements in the economic and business environment in Thailand and discouraged by the lack of progress in Indonesia. As for China, says Matthews, "it's been remarkably stable throughout the whole crisis."

What's fueling the foreign funds' performance is their European holdings. Funds investing only in Europe are up even better. They're up an impressive 17.56% this year, atop 17.8% in 1997 and 24.7% in 1996. The reasons for the rise in Europe resemble those in the U.S.: falling interest rates and corporate restructurings. Also helping are the European Monetary Union and the introduction of the common currency whose debut is scheduled for next year.

The Big Funds' Scorecard

	ASSETS BILLIONS	TOTAL RETURN*
FIDELITY MAGELLAN	\$68.7	13.23%
VANGUARD INDEX 500	55.3	13.26
INVESTMENT COMPANY OF AMERICA	42.3	11.57
WASHINGTON MUTUAL INVESTORS	41.8	12.53
FIDELITY GROWTH & INCOME	40.9	12.24
FIDELITY CONTRAFUND	32.2	11.72
VANGUARD/WINDSOR II	26.6	13.00
FIDELITY PURITAN	23.9	8.38
VANGUARD/Wellington	23.3	8.08
FIDELITY EQUITY-INCOME	23.2	11.74
FIDELITY ADVISOR GROWTH OPP. I	22.8	10.20

*Appreciation plus reinvestment of dividends and capital gains before taxes, Jan. 1 through Mar. 23, 1998

DATA: MORNINGSTAR INC.

"The EMU can be a catalyst for a lot of positive changes that are needed in Europe, like reform of the welfare system and the development of an equity investment culture," says Carol Franklin, who runs the Scudder Greater Europe Growth Fund. "Companies in

Europe are beginning to talk about shareholder value." Laws in several countries have been changed to allow companies to buy back shares, a tactic that has proven powerful in boosting shareholder value in the U.S.

TELECOM TRIUMPH. And just as in the U.S., Europeans are acquiring an appetite for equity investment. "Germans used to invest in bonds, but now they're also buying stocks," says Patrick M. Smith, who manages Pioneer Europe A Fund. "And in Spain, the amount of household financial assets in stocks has gone from 6% to 14% in just a couple of years." Smith has been playing the investment trend by buying shares in European asset-management companies. One of his favorites is Banca Fideuram, an Italian bank that makes most of its money by managing mutual funds. It's up 77% in the past three months and 200% in the past year.

Among the specialty funds, the best showings came from those that hone in

The Worst Performers

The once hot REIT funds cool down, and the bear funds bomb

	TOTAL RETURN*		TOTAL RETURN*
AMERICAN HERITAGE	-22.45%	FIDELITY REAL ESTATE INVESTMENT	-3.76%
ULTRABEAR PROFUND INV.	-18.63	PIONEER REAL ESTATE A	-3.76
PRUDENT BEAR	-17.13	U.S. GLOBAL INVESTORS REAL ESTATE	-3.67
COMSTOCK PARTNERS CAPITAL VALUE A	-11.78	AMERICAN CENTURY REAL ESTATE INV.	-3.63
U.S. GLOBAL INVESTORS GOLD SHARES	-10.53	GRANDVIEW S&P REIT INDEX	-3.53
RYDEX URSA	-10.47	SENECA REAL ESTATE SECURITIES ADMIN.	-3.48
BEAR PROFUND INV.	-10.40	VAN KAMPEN AMER. CAP. REAL ESTATE SECS. B	-3.46
U.S. GLOBAL INVESTORS GLOBAL RESOURCES	-9.70	MORGAN STANLEY U.S. REAL ESTATE A	-3.25
LEXINGTON STRATEGIC INVESTMENTS	-9.02	VAN ECK GLOBAL HARD ASSETS A	-3.23
CAPSTONE NEW ZEALAND	-8.47	STAR SELECT REIT-PLUS	-3.22
LEXINGTON TROIKA DIALOG RUSSIA	-7.83	INVESCO REALTY	-3.19
FRONTIER EQUITY	-7.69	AIM ADVISOR REAL ESTATE C	-3.12
OPPENHEIMER REAL ASSET A	-7.59	VANGUARD SPECIALIZED REIT INDEX	-3.11
WRIGHT EQUIFUND-MEXICO	-7.18	ALLIANCE REAL ESTATE INVESTMENT B	-3.06
GT GLOBAL NATURAL RESOURCES B	-6.69	MIDAS	-2.84
WRIGHT EQUIFUND-JAPAN	-5.99	FEDERATED ASIA PACIFIC GROWTH A	-2.59
ROBERTSON STEPHENS GLOBAL LOW-PRICED A	-5.73	FIRST AMERICAN REAL ESTATE SECS. B	-2.45
CGM REALTY	-5.38	DELAWARE REIT A	-2.37
COHEN & STEERS SPECIAL EQUITY	-4.96	FONTAINE GLOBAL GROWTH	-2.03
WRIGHT EQUIFUND-HONG KONG	-4.75	DAVIS REAL ESTATE A	-1.89
COMSTOCK PARTNERS STRATEGY D	-4.40	UNITED GOLD & GOVERNMENT A	-1.89
PHOENIX REAL ESTATE SECURITIES A	-4.35	SUGEN GOLD	-1.83
COHEN & STEERS REALTY	-4.32	FONTAINE CAPITAL APPRECIATION	-1.79
FLAG INVESTORS REAL ESTATE SECS. A	-4.26	COLUMBIA REAL ESTATE EQUITY	-1.76
MUNDER REAL ESTATE EQUITY INVEST. B	-3.86	FRANKLIN REAL ESTATE SECURITIES I	-1.71

*Appreciation plus reinvestment of dividends and capital gains before taxes, Jan. 1 through Mar. 23, 1998

DATA: MORNINGSTAR INC.

ter should show the strongest inflows in four years

on telecommunications stocks. These funds are up an average 19.79% this year. After several years of just middling returns, telecom stock prices soared, thanks to mergers and takeovers, deregulation in local markets, and an explosion in data-transmission traffic. "All three of those factors drive equipment spending," says Brian B. Hayward, who runs the Invesco Worldwide Communications Fund and is a fan of such telecom equipment makers as Lucent Technologies, Northern Telecom, and CIENA. The best telecom fund so far: Montgomery Global Communications R, up 36.42%, which is taking strength from both the industry boom and the foreign play.

Telecom stocks also played a big part in some of the more diversified funds that made it to the top of the list. Jim McCall, manager of the PBHG Large Cap 20 Fund, says his Lucent shares are up 50% this year alone. That pays off in a concentrated fund with only 20 holdings. Northern Telecom is in the portfolio of the Marsico Focus Fund, the new venture of former Janus Twenty Fund superstar Tom Marsico. Marsico's largest holding, though, is Ford Motor Co., making up 11% of the \$130 million fund. It's no great growth company, but the core auto business sells for four times earnings.

TIGHT FOCUS. Many fund companies are increasingly offering concentrated or "focused" funds—and the quarter's results, at least, show that when they work well, they do stand out. While many funds have a relatively short list of investments when they are small, only the focused funds remain concentrated as they get larger. Not all these funds have "focus" in their name. Transamerica Premier Aggressive Growth has only 24 stocks. "There are so few really good businesses at any one point in time, and when I have one, I make a big bet on it," says Philip Treick, the portfolio manager. Among his top holdings are Dell Computer Corp. and Pixar.

The extreme opposite of the focused fund is the index fund, and managers are finding new variations on a popular prod-

uct. One new company, ProFunds, based in Bethesda, Md., managed to make both the best and worst performers' lists with index-like portfolios. UltraOTC ProFunds uses futures and options to double the return of the NASDAQ 100 Index, NASDAQ's 100 largest stocks. The fund is up 38.76% year to date. UltraBull, designed to double the return of the S&P 500, is up 25.17%. Bear ProFund, designed to perform exactly opposite to the S&P 500, is down 10.4%. UltraBear ProFund, which aims to deliver twice the inverse of the S&P, is down 18.63%.

In addition to a few other bear fund the loser list is dominated by funds specializing in real estate investment trusts (REITS). The sector is down -2.44% for the quarter; the only fund category in the red. In part, REIT prices are sagging because the Clinton Administration is gunning for a treasured tax loophole that benefits a handful of REITS. But Kenneth Heebner, who runs CGM Real Estate Fund, says most likely REITS fell as managers of conservative equity funds traded them in for higher octane stock when the market took off. "There hasn't been any fundamental disappointment in REITS," says Heebner. "And there's been no great change in the outlook either." Heebner argues that relative to the S&P, REITS have never been cheaper: "Double the growth rate at half the price."

Sure, the cheapness of REITS makes real estate funds attractive. But what's even more important is that these funds bring diversification to an investor's portfolio. REIT funds have an even lower correlation with the S&P 500 than foreign equity funds or even many bond funds. That's an undervalued attribute when the stock market's on a winning streak. It will be highly valued when that streak ends.

By Jeffrey M. Laderman
in New York

The Bond-Fund Leaders

TAXABLE FUNDS

	TOTAL RETURN*
PHOENIX EMERGING MARKETS BOND A	9.65%
SCUDDER EMERGING MARKETS INCOME	7.19
FIDELITY CAPITAL & INCOME	6.88
DREYFUS HIGH-YIELD SECURITIES	6.19
BEAR STEARNS EMERGING MARKETS DEBT A	6.17
FIDELITY NEW MARKETS INCOME	6.15
JOHN HANCOCK HIGH-YIELD BOND B	6.02
FIDELITY ADV. EMRG. MKTS. INC. T	5.99
MERRILL LYNCH AMERICAS INCOME B	5.93
GT GLOBAL HIGH-INCOME B	5.78
AVERAGE OF 1169 FUNDS	1.82

TAX-FREE FUNDS

	TOTAL RETURN*
EATON YANCE HIGH-YIELD MUNICIPALS B	2.62%
ALLIANCE MUNI INCOME II VA B	2.41
EATON YANCE AZ MUNICIPALS B	2.05
EATON YANCE NATIONAL MUNICIPALS B	1.82
EATON YANCE FL MUNICIPALS B	1.70
FRANKLIN HIGH YIELD TAX-FREE INC I	1.64
FEDERATED MUNICIPAL OPPORTUNITIES F	1.61
EATON YANCE MUNICIPAL BOND I	1.61
EV MARATHON NATL. LTD. MAT. MUNIS	1.58
FRANKLIN NY TAX-FREE INCOME I	1.55
AVERAGE OF 1348 FUNDS	0.76

*Appreciation plus reinvestment of dividends and capital gains before taxes, Jan. 1 through Mar. 23, 1998
DATA: MORNINGSTAR INC.

The Fund Categories

	TOTAL RETURN*
COMMUNICATIONS	19.79%
EUROPE	17.56
FOREIGN	13.93
LARGE-CAP GROWTH	13.61
WORLD	12.59
TECHNOLOGY	12.32
LARGE-CAP BLEND	11.86
UNALIGNED	11.74
MID-CAP GROWTH	11.42
HEALTH	11.00
LARGE-CAP VALUE	10.79
MID-CAP BLEND	10.20
MID-CAP VALUE	10.04
FINANCIAL	9.64
SMALL-CAP BLEND	9.36
SMALL-CAP GROWTH	9.26

	TOTAL RETURN*
UTILITIES	9.16%
SMALL-CAP VALUE	8.36
DOMESTIC HYBRID	7.22
INTERNATIONAL HYBRID	5.97
DIVERSIFIED EMERGING MKTS.	5.76
PACIFIC/ASIA EX-JAPAN	5.26
NATURAL RESOURCES	3.55
PRECIOUS METALS	2.78
DIVERSIFIED PACIFIC/ASIA	2.01
JAPAN	1.87
LATIN AMERICA	1.33
REAL ESTATE	-2.44
U.S. DIVERS. EQUITY FUNDS	10.93
ALL EQUITY FUNDS	10.05
S&P 500 INDEX	13.17

*Appreciation plus reinvestment of dividends and capital gains before taxes, Jan. 1 through Mar. 23, 1998

DATA: MORNINGSTAR INC.

Scoring telecom stocks boosted the performances of both specialty and diversified funds



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MICRO-CAPS

WERE THE SHORT SELLERS RIPPED OFF?

A California brokerage is accused of manipulating prices

For short sellers of micro-cap stocks, the riches can be substantial—and the risks can be downright scary. These little known market players face a potent weapon: the dread “buy-in,” in which brokerages replace shares sold by the shorts, often forcing them to incur painful losses. The long-short warfare is usually waged in secret, and that is what makes the recent tussle between shorts and a California brokerage, Waldron & Co., so remarkable. This time the shorts have gone public—and the result is a rare picture of how even savvy traders can be slaughtered in micro-cap stocks.

For regulators, who halted trading in the stock at issue, Shopping.com, on Mar. 24, the Battle of Waldron poses a fundamental question. Are short sellers positive forces in the fraud-prone micro-cap market, bringing those stocks down to their true value? Or, as claimed by Waldron, do they hurt investors and brokers by driving down share prices?

The battle began not long after Shopping.com was taken public by Waldron last November, at \$9 a share. The company operates an Internet Web site that is a kind of online warehouse retailer. The shares, trading in the OTC Bulletin Board, climbed instantly to a premium. By early March, the stock was \$32—a market capitalization of more than \$120 million for a company that sustained a \$2.4 million loss on sales of \$377,000 in the nine months that ended last Oct. 31. The company says sales are soaring, but short sellers are unconvinced. “That stock is way overvalued,” says New York short seller John Fiero.

Once the shorts piled on, the buy-ins began. As told by Wal-



NO BARGAIN:

Losses reached
\$2.4 million on
sales of \$377,000

dron's president, Cery B. Perle, what happened was simple: The short sellers failed to deliver the stock they had sold short. He first gave them notice to deliver—insufficient notice, the shorts say. Then, Perle says, Waldron's clearing firm, Wedbush Morgan Securities, went “to the Street” to replace the stock. They didn't have to look far—there was plenty at Waldron & Co. Perle delivered the stock to Wedbush at prices that he concedes were far higher than they had been selling for only minutes earlier. In one instance, the buy-in price charged Fiero was \$39 a share on Mar. 19, when the shares never traded much higher than \$26. The price for the shorts was \$36 on Mar. 11, when everyone else paid \$29 (chart).

Why so high? Well, Perle likens Shopping.com stock to “a 1952 Corvette, pink and white and in perfect condition.... You believe in the next year that Corvette's going to appreciate more.” But he denies Waldron

made a killing on the “Corvette.” He says the shares came not from Waldron's inventory but from “customer accounts.” Asked if he knew the customers, Perle

became agitated, saying: “I'm not going in that direction. I'm going to be very stern with you there.”

But Fiero and other shorts say Shopping.com stock was manipulated upward. Fiero asserts that he lost \$977,000 as a result of the buy-ins, and he feels Wedbush bears much of the blame. “They let Waldron run rampant and rip off other brokerage firms and its customers,” says Fiero. However, Wedbush's head of clearing, Wendy Reardon, asserts that the firm merely acted on Waldron's instructions and committed no wrongdoing. Fiero makes one particularly grave accusation. He maintains that Perle, through an intermediary, recently threatened to buy him in at \$50—double the market price—if he didn't close out his short position. That is denied by Perle.

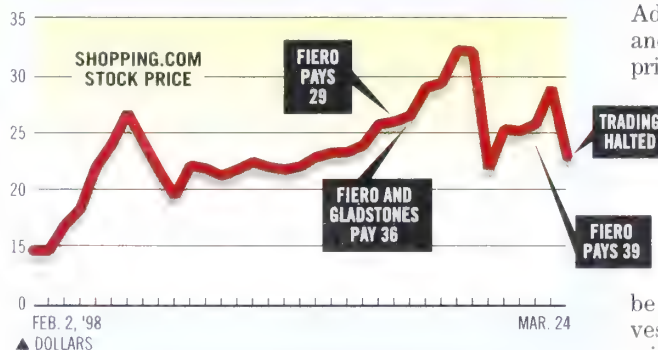
“BRAZEN SCHEME.” Another group of shorts raises serious allegations in a suit filed in U.S. District Court in Manhattan. Florida short sellers Richard and Lauri Gladstone charge that Waldron, Wedbush, and Shopping.com engaged in a “brazen criminal scheme” to manipulate Shopping.com prices by such time-tested methods as failing to execute customer sell orders. The defendants deny wrongdoing.

All the heat has brought forth swift regulatory attention. The National Association of Securities Dealers has launched an investigation of trading in Shopping.com stock, according to sources familiar with the inquiry. And on Mar. 24, the Securities & Exchange Commission halted trading until April, citing “recent market activity in the stock that may have been the result of manipulative conduct.” In a statement, Shopping.com said it is cooperating with the SEC's inquiry.

The NASD and SEC won't comment on the trading halt. But as far as those high-price buy-ins are concerned, Waldron may have some explaining to do. NASD Regulation's general counsel, Alde Adkins, says there are no hard and fast rules dictating the prices at which buy-ins can take place. But he says the prices must be “fair”—and that the person who sets the price must be prepared to defend it. This is one battle, it seems, that the short sellers are likely to win. But whenever prevails, there will still be sure losers—the small investors who get caught in the middle.

By Gary Weiss in New York

SLAUGHTER OF THE SHORTS



DATA: BLOOMBERG FINANCIAL MARKETS, BUSINESS WEEK

GOOD.

THE S&P 500 INDEX		
1 Year	3 Years	5 Years
33.3%	31.0%	20.2%
Average Annual Returns As Of December 31, 1997		

BETTER.

AMERICAN CENTURY 5-STAR PERFORMANCE				
Average Annual Total Returns As Of December 31, 1997	1 Year	3 Years	5 Years	Life of Fund
INCOME & GROWTH FUND	34.5%	31.7%	20.4%	21.1% (December 17, 1980)
EQUITY GROWTH FUND	36.1%	32.6%	21.0%	19.0% (May 9, 1991)
Morningstar Ratings As Of February 28, 1998. Funds Rated For The Overall Period Among 2,383 Domestic Stock Funds				

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COMMENTARY

By Amey Stone



BAD QUARTER? DON'T KEEP SHAREHOLDERS GUESSING

Investors used to just have earnings season to worry about. Now there's also pre-earnings season to sweat over. The number of companies publicly announcing that first-quarter earnings won't meet Wall Street's expectations has been steadily increasing over the past few years. Investors benefit from these "pre-announcements," since they are getting new information earlier. But the way in which some companies handle the announcements leaves much to be desired.

As of Mar. 25, First Call Corp., a Boston firm that tracks earnings estimates, tallied 203 pre-announcements for this quarter, with about 54% reflecting lower expectations. March brought bad news, first from



such tech leaders as Intel, Motorola, and Compaq Computer and then from Kimberly-Clark, Sunbeam, and Cummins Engine. Despite the positive news from Microsoft on March 24, "what really stands out about this quarter is that there have been so many significantly negative announcements from major companies," says Charles L. Hill, First Call's director of research.

SHOCK ABSORBERS. The public releases are a vast improvement over the days when companies might just tip off a few favored analysts to lower their numbers. That allowed some well-connected investors to bail out of a stock before most others realized anything had gone awry. To be sure, the warnings can cause sharp sell-offs, but they



seem to help smooth things over by the time the actual earnings number is released.

To disseminate disappointing earnings forecasts this quarter, companies have used a range of methods that in some cases can be improved upon. Some, such as Intel and Cummins Engine, issued press releases. Others, including Compaq Computer Corp., followed the press release with a conference call but restricted it to analysts and big investors. Walt Disney Co. didn't issue a release at all but guided a few analysts to lower their expectations for the fiscal second quarter, prompting a 2.8% slide in the share price on Mar. 4. The company says that it just responded to analysts' questions and did not consider it had "material" news to report, which would have necessitated a public release.

Disney may be right, according to the letter of the law. Learning that the box-office take was weaker than expected did not prompt analysts to lower their earnings forecasts by much. However, the spirit of the law would call for Disney to have issued a press release, giving all analysts and investors the same information at the same time.

This gap between spirit and letter is something the Securities & Exchange Commission has taken note of recently. "Legally, you

can split hairs all you want," said SEC Chairman Arthur Levitt Jr. in a Feb. 27 speech warning analysts not to trade on material information prior to its public release. "But ethically, it's very clear," Levitt noted "a great deal of unusual trading" can occur before announcements.

Leaving legal gray areas aside, there are some simple things companies should do to improve the flow of information. For openers, companies should pre-announce earnings only after the market closes, granting the public ample opportunity to learn the news before trading resumes the next day. This is increasingly the practice, but it should be the rule.

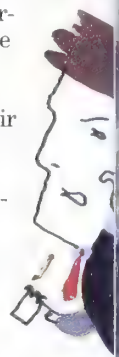
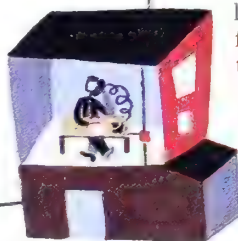
ALL EARS. If companies are going to hold a conference call to provide more detail about the news release, they should open it up so the public can listen in. This can be done by broadcasting Q&A sessions live over the Internet. Microsoft recently started doing this with its quarterly earnings announcements, and Intel will do so with its next announcement. For those companies with Web sites in place, this is neither an expensive nor complicated proposition. Companies can also open up their conference call to the public by announcing the number in their press release.

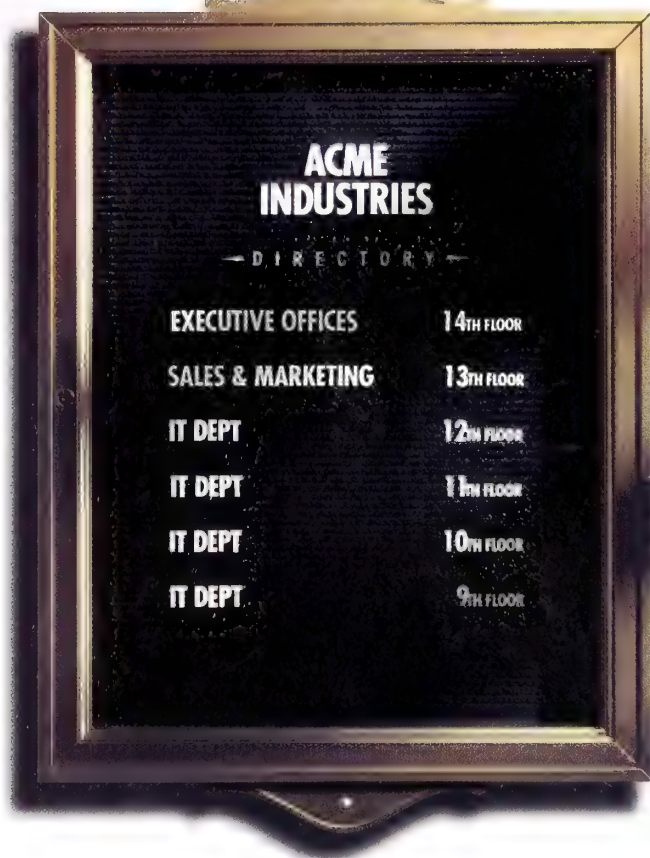
Technology

now allows thousands of listeners in on a single call.

Pre-announcements may only smooth the overall effect of a company failing to meet earnings expectations. Ultimately, the stock price will settle at its real economic value. Still, with many investors looking for signs it may be time to take profits, companies should provide Wall Street and the general public with the same information at the same time.

Stone writes about Wall Street for Business Week Online.





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BY GENE G. MARCIAL

IS CITICORP EYEING PAYMENTECH?

The rising tide hasn't lifted all stocks. Some have gone south, like Paymentech (PRI), the nation's third-largest processor of merchant credit-card transactions. Its shares have been on the ropes since it disappointed the Street last year with lower-than-expected fiscal

fourth-quarter earnings. Up as high as 34 in mid-June, the stock fell as low as 12 in late December. But it's now rebounding, snapping back to more than 17 a share on Mar. 24.

Most analysts are still skeptical, but at least one—Gregory Gould of Goldman Sachs, has raised his rating from "market

perform" to "market outperform."

That doesn't seem like a significant upgrade, but some big investors argue there's another reason to be upbeat on the stock: whispers that the company is being shopped.

These pros say Banc One, which owns a 57% stake in Paymentech, plans to sell its holdings. The bank ended up with a big slice of the stock when it acquired Paymentech's parent, First USA, in June, 1997. Banc One officials, say some analysts, have said they plan to unload the Paymentech shares at some point. A spokesman says in order to maintain the pooling-of-interest nature of the acquisition, Banc One has to keep its stake for two years after the closing of the deal. But that does not preclude a sale prior to June, 1999.

Whispers are that Banc One is talking with Citicorp and at least one other financial institution to unload the block. One New York money adviser recalls that Citicorp officials had privately expressed interest in buying Paymentech when it was still part of First USA. Paymentech, called First USA Paymentech then, changed its name after the acquisition.

"Paymentech continues to face pricing pressure and is having a tough

time making acquisitions—which had been a big source of growth in the past," says analyst Jennifer Scutti at Prudential Securities. A shareholder class action also has been filed against Paymentech in Texas, claiming it failed to disclose the slowdown resulting from its acquisition by Banc One. Paymentech denies the allegation. A Paymentech spokesman declined comment on the Citicorp rumor. Citicorp didn't return calls.

RECOTON'S GOOD VIBRATIONS

Investment manager Douglas Raborn, who manages some \$120 million for wealthy clients, has bagged some huge winners, such as Great Western Financial, which he bought last year at 26 and sold at 48 after six months, and Maytag, which ran from 22 to 49. Now he says he has found another: Recoton (RCOT), a major supplier to Circuit City Stores and Best Buy, retailers of electronic products.

Recoton, a leading developer and maker of consumer-electronics accessories, sports fundamentals that Raborn goes for: Strong earnings growth and a low price-earnings ratio. Recoton currently trades at 23, or at a p-e of only 10 based on Raborn's 1999 earnings estimate of \$2.25 a share. This year, Raborn expects earnings of \$1.85, vs. 1997's \$1.18.



WINNING STRAIGHT: Raborn likes the low Recoton p-e

big customers, such as Sears Roebuck, to market its line of loudspeakers—including Advent, AR/Acoustic Research, and Jensen products. This line alone, says analyst William Jelin of Pauli & Co., should add at least \$15 million in sales volume per year. Recoton also has signed recent agreements with other big retailers, including Wal-Mart, Kmart, OfficeMax, and MusiLand Group.

Raborn says that in spite of the shakeout now among retailers of electronic products and video games, Recoton will prevail as a major supplier to the industry's survivors. Meanwhile, the company is pursuing some new businesses with its

A LAB PREGNANT WITH POSSIBILITY

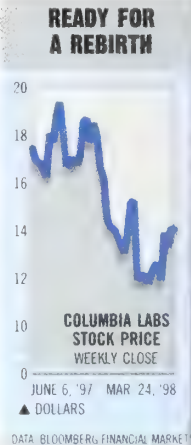
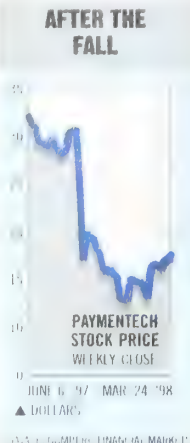
Insiders at Columbia Laboratories (COB) think its one "blockbuster" product—Crinone, a natural progesterone gel approved in 1997 by the Food & Drug Administration for infertility treatment—is finally ready to take off. Its marketing by American Home Products' Wyeth-Ayerst unit is now being launched "in full force in the U.S.," says Columbia Labs Chairman William Bologna. He's convinced Crinone will highlight Columbia's focus on women's health care, a market valued by analysts at \$6 billion and expected to exceed \$10 billion by 2000.

Crinone comes in two forms: Crinone 8%, a prescription product approved for assisted reproduction, launched last September in 23 fertility clinics, which analysts say, has had solid acceptance and Crinone 4%, launched in mid-March, said to be a breakthrough in hormone-replacement therapy.

Columbia uses a patented bioadhesive applicator that delivers Crinone directly to the uterus. The gel adheres for at least 72 hours and protects against infection, minimizes leakage, and is hypoallergenic. Analyst Elizabeth McCreery of Lazard Frères expects Crinone 4% to become an "important option" for hormone replacement, offering advantages to progestin-intolerant women and women in early and midstages of menopause.

McCreery expects earnings to increase from 3¢ a share in 1997 to 3¢ in 1998, \$1.07 in 1999, and \$1.68 in 2000. Columbia's stock, trading at 1 could hit 21½ in 12 months, she says based on a p-e of 20 times her 1999 earnings estimate.

Bologna puts the Crinone 4% market at \$1.5 billion. "We expect to take some 2% of the Crinone 4% market this year and then ramp it up next year," he adds. AHP doesn't own shares in Columbia. "We haven't discussed that aspect," insists Bologna.



E'S BIG. HE'S UPSET. E'S INVISIBLE

Merchandisers are antsy about *Godzilla's* marketing

It was the end of a long day of shooting on the north shore of Oahu. Matthew Broderick, star of the Sony Pictures Entertainment *Godzilla*, stepped off a seaplane and headed into the brush in search of the giant lizard. But for Dean Devlin, the film's 35-year-old producer, one task awaited. As shooting finished, he headed across the island to the lavish Ihi Lani resort to brief the Taco Bell executives on *Godzilla's* totally secretive marketing plans. They needed was someone to hold the hand a little," says Devlin.

It's not the movie they're worried about. If Hollywood buzz is to be believed, *Godzilla* is going to be a monolith this summer. But pardon the marketers and licensees who, like

Taco Bell, have signed on to create movie tie-ins for getting a little buzz. Until the film opens on May 20, none of them will be able to see the image of the rampaging lizard to promote their products. Toys, no toys, no plastic soft-drink cans appear if they see *Godzilla*. Says W. Wayne Booker, senior vice-president of marketing for Trendmasters Inc., a St. Louis-based toymaker, "The rights to *Godzilla* are more than 40 years old. *Godzilla*-based toys: one was O.K. with at least not at

at's understanding since the tactic is as far from standard Hollywood marketing as a movie can be. Normally, movie marketers try to build excitement and merchan-

dise sales for a film by trotting out its stars well in advance of opening day. Walt Disney Co. has made a science of the practice and has been rewarded with successes such as *The Lion King's* \$100 million in toy sales.

So why keep the big guy under wraps? The mystery marketing is the brainchild of Devlin and director Roland Emmerich, the team that created the 1996 Twentieth Century Fox Film Corp. blockbuster *Independence Day* using a similar no-see-um tactic. The two have redesigned *Godzilla*, the star of more than 20 B-movies—and have mandated that no one outside the production team can spot him in his full glory till opening night. Devlin and Emmerich hope to create a mood similar to the opening weekend of *Inde-*

pendence Day, when moviegoers flocked to get a look at the much-heralded bad guys. That success persuaded Sony to go along with the unorthodox approach for *Godzilla*. "With filmmakers of this quality, you'll take a chance," says Sony Chairman John Calley.

Still, it's a pretty big roll of the dice. Licensing experts estimate that as much as 30% of a movie's tie-in products are sold before a film's opening weekend via fast-food restaurants, toy stores, and the like. That makes hiding *Godzilla* from the public eye a 22-story headache for the retailers. Despite complaints from Toys 'R' Us Inc., for example, stores won't be allowed to stock *Godzilla* toys until the night before the movie debuts. Bob Weinberg, the chain's senior vice-president and general merchandising manager, complains that stores could easily be selling *Godzilla* merchandise over the next several weeks. "We think it's all kind of silly," he says. "You don't have much of a *Godzilla* display without *Godzilla*."

BODY PARTS. But having struck this deal with the filmmakers, the movie's marketers and licensing partners are making the best of it. Taco Bell, which will spend \$20 million to promote the film, made two separate TV commercials—one for April that shows only the lizard's giant foot smashing New York, and a later version with a full view of the rampaging beast. Eastman Kodak Co., which has a product appearing in the flick, had to let a Sony production crew film its commercial. And Trendmasters played up the secrecy by posting guards outside its display space at trade shows, issuing card keys to a select few retail buyers.

Sony, too, is looking to make a virtue of this necessity. Although theater trailers have been running since January, they have built curiosity by never showing more than the tail, foot, or eye of the beast. Sony has also coughed up roughly \$20 million for a high-profile TV ad campaign—including an estimated \$2 million for a spot on the upcoming

WHAT PRICE SECRECY?

*Movie tie-ins typically tally 30% of their sales before opening day, leaving many marketers nervous about Sony's efforts to keep its new *Godzilla* under wraps:*

TACO BELL Filmed two separate ads. Early ads show only *Godzilla's* feet stomping New York City; the beast himself won't appear till opening day.

TOYS 'R' US Can't put *Godzilla* merchandise on its shelves until the film debuts.

KODAK To preserve secrecy, Sony insisted on using its own film crew to shoot Kodak's ad promoting a camera tie-in.

TRENDMASTERS Allowed only a handful of retailers to view toymakers' prototypes, limiting industry buzz and early demand.





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finale of *Seinfeld*. And at 150 movie theaters, Sony will put up 10½-foot-tall computerized displays recreating a stormy weather scene in the movie in which New York is trashed—with no monster in sight. Says Sony marketing chief Robert Levin: "We were forced to get creative."

For some, however, the extra effort wasn't worth it. Sony says Galoob Toys Inc., which makes toys for movies such as *Star Wars*, backed out of an oppor-

solid reputation—and it already has rights to make classic Godzilla toys—licensing heavyweights like Mattel and Hasbro didn't sign up. Burger King Corp. chose to stick with its summer movie tie-in, *Small Soldiers*, rather than add *Godzilla*. Altogether, *Godzilla*'s marketers have signed tie-ins with 80 licensees. While certainly good, the numbers trail the partnership deals typically signed up by movies with more traditional marketing; *The Flint-*

restrial generated interest by hiding the face of their alien star until opening night. And *Godzilla* may have a way to make up for lost face time, says Jo Krier, president of Exhibitor Relations Co., which advises theaters on upcoming films. With the field to itself, should enjoy a blockbuster opening weekend. "Everyone else is afraid *Godzilla* and has moved their films other weekends to stay clear of it," Krier says.

"We think it's all kind of silly. You don't have much of a *Godzilla* display without *Godzilla*"

tunity to be *Godzilla*'s toymaker. Galoob declined comment. And already, some *Godzilla* licensees are suffering for the silence. The line of *Godzilla* toys isn't creating nearly the same buzz with retailers as the Hasbro line based on Dreamworks SKG's *Small Soldiers*, says Martin Brochstein, executive editor of *The Licensing Letter*. That's a problem, since many sellers finalize their Christmas orders in spring and summer.

Moreover, while Trendmasters has a

stones, for example, signed more than 100 partners. And although overall merchandise sales are hard to estimate before a picture opens, industry experts predict that on toys alone, *Godzilla* will take in between \$50 million and \$75 million—well short of *The Lion King*'s record.

Can secrecy help *Godzilla* beat those ho-hum predictions? Mystery has made stars out of other monsters. In addition to the evil aliens of *Independence Day*, the producers of *E.T.: The Extrater-*

Walt Disney Co. studio chairman J. Roth scheduled his summer action movie *Armageddon* for July, in part to stay out of *Godzilla*'s way. "[*Godzilla*] has a chance to do \$100 million to opening weekend," he says.

Sony is already planning to turn the giant lizard into a franchise, with more films down the road and an animated TV series. Of course, that assumes he's a hit when he finally shows his face.

By Ronald Groves
in Los Angeles

Readers Report

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EDITED BY CATHERINE ARNST

SCIENTIFIC JOURNAL—OR VANITY PRESS?

ON MAR. 16, NYMOX PHARMACEUTICAL CORP., a small company in Montreal specializing in Alzheimer's disease research, claimed it had discovered a possible cause of the disease. It published its findings in the March issue of the *Journal of Alzheimer's Disease*. Publication usually confers legitimacy on scientific research—but maybe not this time.

The brand new *Journal of Alzheimer's Disease* was started in part with a grant from Nymox to the journal's publisher, IOS Press. The journal's editor, Dr. Carl R. Merrill of the National Institutes of Health, is a consultant to Nymox. The journal's 23-member editorial board includes six people who either consult for Nymox or have published with its scientists, according to Nymox scientist Hossein Ghanbari.

Ghanbari and Nymox CEO Dr. Paul Averbach both insist that they don't control the journal or its editorial board members. The publication is "absolutely independent," says Ghanbari.

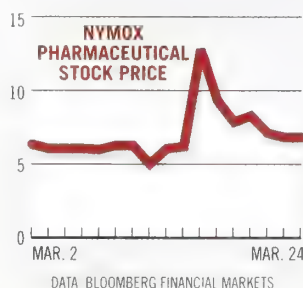
Nymox says it has discovered tiny protein balls called "spherons" that swell and eventually explode in the brains of Alzheimer's sufferers. Before the article appeared in the *Journal of Alzheimer's Disease*, Nymox submitted it to the prestigious scientific journals *Science* and *Nature*, says Ghanbari. Both turned it down, and some scientists say there was good reason to do so. "That data is extremely

weak," says Peter T. Lansbury Jr., a Harvard Medical School neurologist. "Any less data and there would be no data."

Scientists may have been skeptical, but not investors. Nymox' stock doubled, to \$12.75, following the Mar. 16 release of the findings. But by Mar. 24, the stock was back to 6 $\frac{3}{4}$ ¢ on NASDAQ.

This isn't the first time Nymox has been accused of questionable practices. In 1996, it was criticized for running ads for a test it developed for Alzheimer's before publishing data to show whether the test worked. Nymox now says it is testing drugs to combat the problems "spherons" cause. Lab tests are under way, and human trials could follow. *Joseph Weber*

NEWS HITS NYMOX



FOR THE SMALLEST VALVE, THE SECRET IS BALANCE

A MIGHTY MICROVALVE THAT controls the flow of gas could open a flood of new products, from a higher-tech version of pump sneakers to airline seats that adjust the contours of your body.

Invented by BCAM International Inc. of Melville, N.Y., the patent-pending valve is part machine, part computer chip. It is about one centimeter wide and is made of silicon. Production versions will have sensing and control circuitry etched into the surface. Its mechanism is a minuscule flexible silicon plank that bends up to close off air flow and bends down to open it. The trick is that the air pressures pushing on the two sides of the plank are balanced, so it takes very little power—about 15 milliwatts—to keep the valve either open or closed. The main valve is nudged in either direction by opening or closing a flap that controls the pressure of air against the bottom of the plank. That flap is just 100 nanometers across—about the width of a human hair.

BCAM says its microvalve is smaller, consumes less power, and is potentially cheaper to manufacture than its main competitor, the Fluistor valve from Redwood Microsystems Inc. of Menlo Park, Calif. Redwood, though, says its microvalves permit greater accuracy and can handle a wider range of pressures.

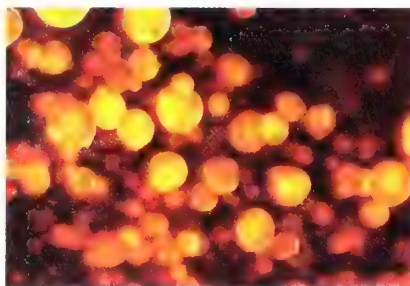
BCAM says the valve will probably be used first in footwear, including cushioned shoes for diabetics, who are prone to pressure sores. For the medical-equipment industry, a smart microvalve could be embedded in a disposable drug-inhalation device to ensure that patients receive the proper dose. *Peter Co*

THESE MOLECULES ARE REAL SELF-STARTERS

FOR ENGINEERS, IT'S CLOSE TO playing God. They are devising so-called self-assembly techniques aimed at getting molecules to arrange themselves into larger functioning systems, much as eggs and sperm self-assemble into human beings. Until now, only nature has been able to get more than a few molecules to join together, into very small nanostructures. But on Mar. 20, two University of Rochester researchers said they had developed the largest synthetic structures ever made by self-assembly.

Though each structure contains millions of molecules,

the largest is only 50 microns long, less than the width of a human hair. Still, that's 1,000 times larger than the previous record for synthetic self-assembled structures, the researchers report in the journal *Science*. "In the world of self-assembly, these structures are giant," says X. Linda Chen, one of the researchers and a graduate engineering student at Rochester. Chen and engineering professor Samson A. Jenekhe started with a large polymer macromolecule long thought too unstable for self-assembly. They tamed the polymer by inserting hydrogen bonds into the structures, the same stabilizers found in



'GIANT' STRUCTURES: A photo of self-assembled, hollow spheres

DNA and other natural self-assembled proteins.

The molecules form a variety of shapes, including spheres, cylinders, rings, and disks—all of which have a fluorescent glow. The researchers say the structures could be utilized as drug-delivery vehicles, adhesives, lasers, sensors, and for other industrial applications. □

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THE TAX MAN YES THE NET

House bill could sort out who will owe what to whom



during a recent visit to California, Utah Governor Michael Leavitt went online to order some food for delivery to his home. His In-account was set up in Utah, the was based in New York, and the were shipped from New Jersey. he have to pay sales tax to one of states? All of them? Or none? h Internet sales expected to surge he next decade, the answer will ically important to both states and who do business on the Web. To here are no clear rules setting out if anyone—should get those bucks. d, a crazy quilt of ad hoc taxes is ing to plague E-commerce. a new congressional initiative may set some ground rules for both

Internet and mail-order sales and resolve what could easily grow to a \$20 billion controversy. The deal, proposed on Mar. 19 by Representative Christopher Cox (R-Calif.) and backed in principle by House GOP leadership and the White House, would require major trade-offs by both Net sellers and states. While Cox's plan will undergo alterations, it seems likely that Congress will act this year. And the proposal dramatically shifts the tone of the debate. "This thing has a pretty good chance of passing," says Frank Kelly, a vice-president at Charles Schwab & Co., which does much of its business on the Internet.

Under Cox's plan, industry, which now happily avoids most levies on Net sales, would agree to participate in a process

that could lead to widespread taxes on E-commerce within three years. In return, it would get a consistent, 50-state regime of taxation. Net sales would be taxed at the same rate as mail order or Main Street transactions. And while states could set their own rates, each sale could be taxed only once. That would prevent a seller's state and a buyer's state from trying to tax the same sale. The details of Net taxation would be settled by a panel of industry and government officials that would send its recommendations to Congress by 2000.

For their part, states would accept a three-year freeze on new taxes on Net sales, as well as a permanent ban on taxing the monthly fees charged by Internet service providers. What's in it for the states? An end to the uncertainties that have dogged their efforts to tax both Internet and mail-order sales.

FAIR DEAL. In recent years, the battle over cybertaxes has sowed widespread confusion. Texas wants to tax Internet access fees for travelers who log on during brief stays in the

state. California revenue officials argue that a company that has a Web page on a server located in their state would be required to collect California sales tax for purchases made on the site. Such revenue grabs have persuaded much of industry to accept the certainty of taxation in return for simplicity and equal treatment. "We want to make sure there is a fair, nondiscriminatory system," says Jill Lesser, deputy director for law and public policy at America Online Inc.

The Cox bill has widespread political support, though disagreements remain over details. But the plan has deeply divided business. Catalog sellers—who generally don't have to charge a tax on their products—see it as a backdoor way to hit them with new levies. "This seems some-

EBERTAX SOLUTION?

Representative Christopher Cox (R-Calif.) has offered one answer to the Internet tax question. His approach would:

permanently ban
ral taxes on
Net and Net
merce, and
ibit state taxes
Internet access

► Place a three-year
freeze on any new
state taxes on Net
purchases, thus
avoiding a crazy quilt
of taxes

► Give a commission
two years to propose
ground rules for
future state taxes
on Net commerce
and on catalog sales

► Require that any
tax be paid only once,
with no distinction
between Net sales
and traditional
retail sales

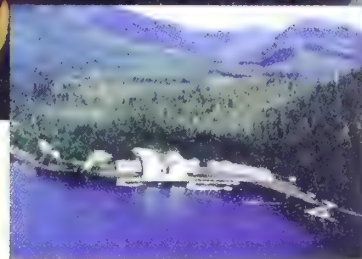
► Ban tariffs or
other international
levies on cross-
border E-commerce

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devious," gripes Robert Edmund, of Edmund Scientific Co., a Bar- (N.J.) direct seller of scientific ment and optics. "We're looking at o of the iceberg here."

the other side are Net sellers, who to be treated the same as their order rivals. State tax experts say ave a point: "If there is going to olution, it should address the entire of interstate sales," says Michael H. an, a partner and tax expert at tant KPMG Peat Marwick.

re's no doubt that for now, mail is where the money is. According Direct Marketing Assn., catalog totaled more than \$78 billion last No one knows how much business one on the Net, though the White estimates perhaps \$4 billion. But tential for growth of online sales is ous. International Data Corp. pre- hat Net sales will top \$200 billion 02. That translates into more than llian a year in potential state sales Throw in an additional \$4 billion ould be collected from mail orders, ates could hike their sales tax base taggering 10% to 15%.

ernors argue that taxing Net and g sales is only right. After all, why a local department store have to a 5% sales tax on a shirt while End can duck the levy by selling ame garment over the phone or gh its Web site? Says Colorado nor Roy Romer: "The tax should pend on the way you buy it or whom you buy it."

E "PRESENCE." For more than 30 however, the Supreme Court has different view. It insists that only unies with a physical presence in a should be required to collect sales But the court has invited Con- to find a way for states to impose ble taxes. Until now, it never tried. ch mail order, such presence has easy to define. But E-commerce aised issues that the courts never oated. Does the location of a com- server count? Says Mark Neber- vice-president for tax policy at the are Publishers Assn.: "There's a ain of uncertainty."

e battles over whether each indi- l state will choose to tax Net actions—and what they'll do with money—won't be fought in state atures until 2000. But for Wash- n, passage of the Cox bill would t a new reality: For all their flash promise, sales on the Net are no ent from selling a yo-yo at the nd-dime.

Howard Gleckman in Washington

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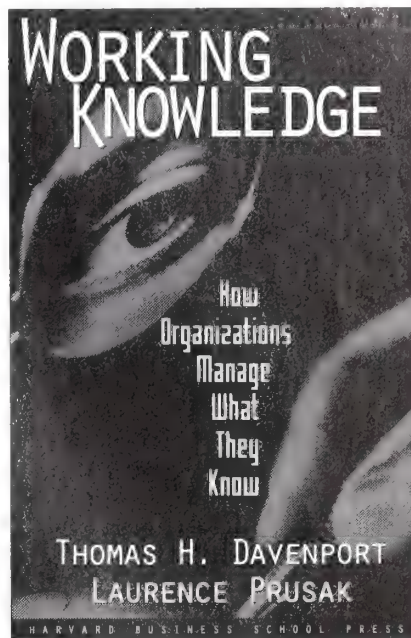
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EDITED BY AMY DUNKIN

GOING GLOBAL: IS IT TIME TO TAKE THE PLUNGE?

For many years, the conventional financial wisdom held that American investors should place 10% to 20% of their portfolios overseas. But over the past year, with the U.S. stock market skyrocketing and many foreign markets blowing up, the maxim doesn't sound very sage-like. Remember the Asian markets' meltdown of last fall or the Latin collapse a few years earlier? Why take the risk of sending your money abroad when there's so much to be made at home?

Despite last year's debacle in the Asian markets, now's not the time to toss aside the advice. That's because it should continue to apply over the long run. A compelling combination of long-term economic fundamentals and short-term market conditions suggests that now is an

opportune moment to broaden your investment horizons. Many overseas markets appear poised for a strong upturn. "If you look at valuation levels and growth prospects, maybe people should put a bit more than 20% of their portfolio internationally," says Robert Furdak, director of international strategies at Numeric Investors, a Massachusetts-based money management firm.

For most individual investors, the easiest way to get access to foreign equities is through mutual funds. Professional money managers, many of whom have analysts working around the world, can offer an edge when it comes to dealing with unfamiliar markets and exotic economies. In fact, so far this year, foreign-stock mutual funds have gained 13.93% vs.

13.17% for the Standard & Poor's 500 index, according to Morningstar Inc. A good number of closed-end funds that invest abroad are selling at substantial discounts to their net asset values, making them attractive investments.

COPYCATS. The history of stock markets shows they are cyclical, with fat years eventually followed by lean ones. By almost every measure, U.S. stock market valuations are higher than just about anywhere else in the world. Shifting some of your assets overseas is one way to temper any dam-

age that a plunge in the Dow Jones industrials might do to your portfolio.

But there's an even better reason for going abroad. Many foreign companies are emulating the practices of U.S. corporations by restructuring and reengineering their businesses. "A lot of the things American companies have been doing to improve

efficiencies and operations are

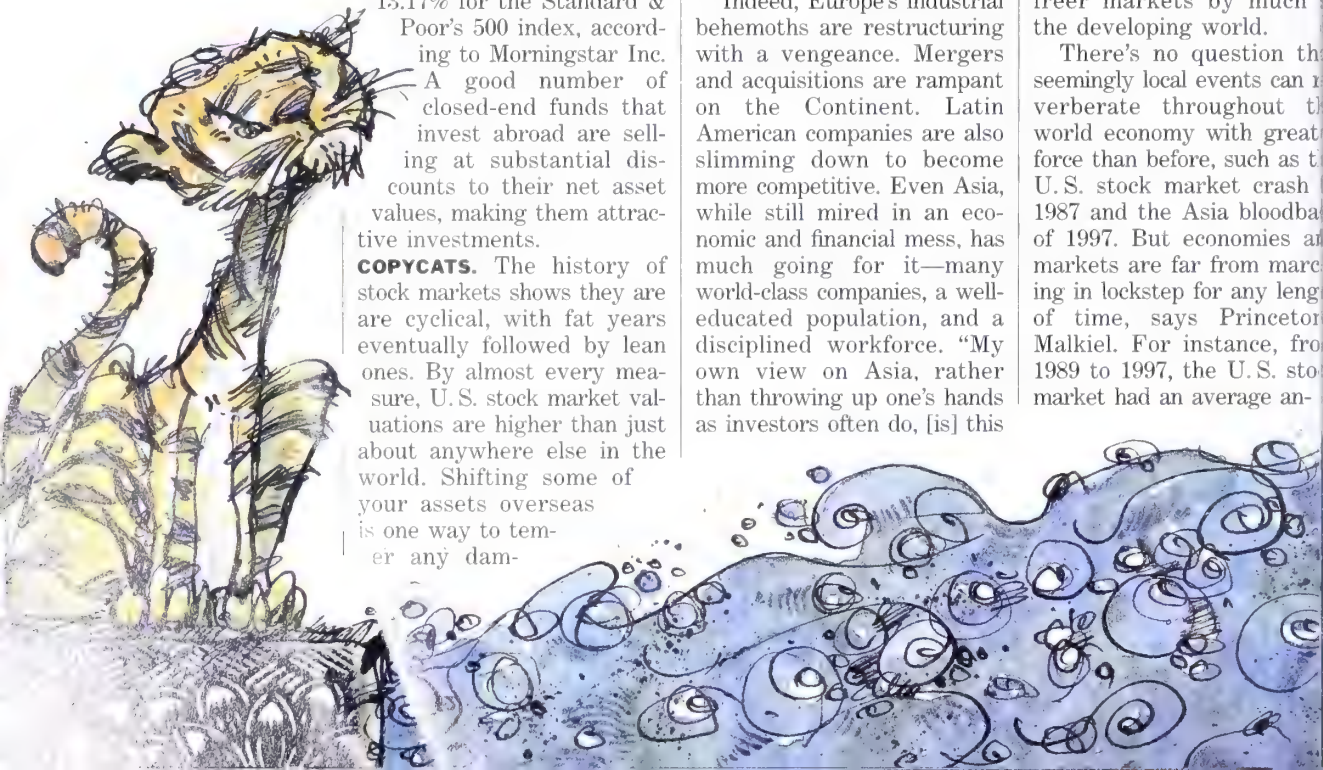
only starting to take place in some foreign markets," says George Murnaghan, managing director of Rowe Price-Fleming International, the mutual-fund company. Adds Laurence Siegal, director of policy research in the investment division of the Ford Foundation: "The rest of the world isn't going to sit on its hands while the U.S. runs away with all the money."

Indeed, Europe's industrial behemoths are restructuring with a vengeance. Mergers and acquisitions are rampant on the Continent. Latin American companies are also slimming down to become more competitive. Even Asia, while still mired in an economic and financial mess, has much going for it—many world-class companies, a well-educated population, and a disciplined workforce. "My own view on Asia, rather than throwing up one's hands as investors often do, [is] this

is precisely the time the international diversification makes sense," says Burt Malkiel, professor of finance at Princeton University and author of *Global Barga* (Simon & Schuster, \$25). Notes Campbell Harvey, professor of finance at Duke University, "The really big returns in Asia provide investors with an opportunity

Problem is, international diversification is a tarnished idea these days. Any U.S. equity investors who did the prudent thing and diversified overseas over the past decade got lower returns for the effort compared with an investor who kept everything at home. Skeptics argue the benefits of international diversification are shrinking. The bonds trade and capital are stronger after the end of the cold war and the embrace of freer markets by much of the developing world.

There's no question that seemingly local events can reverberate throughout the world economy with greater force than before, such as the U.S. stock market crash in 1987 and the Asia bloodbath of 1997. But economies and markets are far from marching in lockstep for any length of time, says Princeton's Malkiel. For instance, from 1989 to 1997, the U.S. stock market had an average an-



return of 16.6% compared with a -7.3% return for the Japanese stock market, according to figures compiled by Watson Associates.

The good news for international diversification is that the forces are offsetting the move toward tighter correlations between markets. Political and cultural barriers between nations are still formidable. Large parts of many economies remain relatively insulated from international competition. Monetary and fiscal policies can diverge widely. "Statistically, correlations between markets are somewhat closer than they have been," says Murphree of Rowe Price-Fleming International.

Most important, overseas diversification has worked as a risk reduction strategy. For example, between 1970 and 1994, the Standard & Poor's 500 stock index had an average annual return of 13%. But the volatility of the index, measured as its standard deviation, averaged 17.3% a year. Over the same period, a portfolio composed of 70% U.S. stocks, 10% international stocks, and 20% long-term government bonds returned 12.5%—only a fraction less than an all-U.S. equity portfolio—while boasting a far lower volatility level of 14.1%. International diversification is not a flight to safety. Fund manager Rowe Price-Fleming views the returns a very different way. It uses moving averages to measure the return on a

The Case for Investing Abroad

THE KEY POINTS

► The U.S. stock market has sizzled while the rest of the world has simmered. The risk/reward ratio currently favors plunging down some money overseas.

► Diversification pays. Unless there is a worldwide economic shock, stock markets don't move in lockstep over the long run.

► Investors can buy shares in some terrific companies at good prices, such as Japan's Konica, France's AXA-UAP, Brazil's Telebrás.

► The crash of the Asian markets presents some excellent buying opportunities.

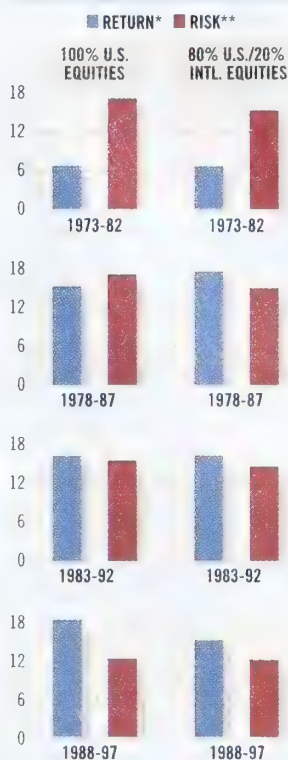
► Some closed-end country funds are trading at big discounts to net asset value and are particularly attractive right now.

DATA: BUSINESS WEEK

100% U.S. stock portfolio with a portfolio that's 80% in U.S. stocks and 20% in international equities (chart). With the exception of the past several years, the diversified portfolio performed a tad better and with less risk.

Many economists say that people may be taking the wrong lesson from recent ex-

HOW FOREIGN STOCKS HELP



*Average annual

**Variability of return as measured by standard deviation

DATA: ROWE PRICE-FLEMING, BUSINESS WEEK

periences with overseas investing. They note that while many investors took their money abroad, they failed to diversify it enough. In 1994, for example, a huge chunk of all U.S. overseas investment went to two countries, Mexico and China. Another common misstep is to diversify among countries within the same part

of the world. The recent Asian debacle is strong evidence that regional effects are fairly strong. "Don't take 20% of your portfolio and bet" on a single region, says Duke University's Harvey.

BEHEMOTHS. Another popular strategy is to buy shares in Coca-Cola, Gillette, Procter & Gamble, and other U.S. multinational behemoths. Those giants, which operate in scores of countries, are certainly poised to benefit from global growth. But the share prices of the American multinationals are so influenced by the ups and downs of the U.S. stock market that they really don't provide all the advantages of international diversification. "If you really want diversification, you have to take a deep breath and take the plunge into markets all over the world," says Nariman Baravesh, chief international economist at S&P DRI.

To be sure, there are lots of risks associated with going overseas. Countries can devalue their currencies or clamp on capital controls. Accounting standards are weak and economic information poor. Political instability is a fact of life. Emerging markets are extremely volatile. Nevertheless, for long-term investors, the strategy that seems to make the most sense in a global economy is a global one.

Christopher Farrell



A PIECE OF REAL ESTATE FOR A PITTANCE

Wall Street has come up with a new way to invest in real estate without paying a

commission. Several firms are packaging real estate investment trusts (REITs) into what are known as unit investment trusts (UITs), or fixed portfolios with a limited life. Unlike mutual funds, these baskets of stocks don't change at all from the time they are created until they dissolve, typically in two years.

Brokers sell the trusts without a load during the initial offering period, which lasts about three weeks. That makes these units a good deal if you get in early. They're also attractive if you have only a small amount to invest: Salomon Smith Barney's trusts have a minimum of only \$300, and Prudential Securities asks for \$250 for retirement accounts. Anyone who wants to buy into a trust after the offering period must do so in the secondary market and pay an upfront charge, usually 4%. The trusts currently have annual dividends of about 6% and are down a few percentage points this year but most compare favorably to the 4% slide in the Wilshire REIT Index in 1998.

NEW PLAYERS. The UIT sponsor can forgo a commission because it gets stock from the REIT at about a 5% discount. Salomon Smith Barney was the first firm to structure such a deal last fall, followed by Prudential Securities, Legg Mason Wood Walker, and Nike Securities, a Chicago-area firm that specializes in UITs. All completed second trust offerings this year. J.P. Morgan, J.C. Bancorp, and J.C. Bancorp have also gotten into the act

recently. Van Kampen American Capital, which sells through independent financial advisers, currently has a new REIT trust with a \$1,000 minimum in the no-load phase. Its REIT Income and Growth Trust, Series 1 will be priced on Apr. 9. "Everybody is jumping on the bandwagon," says Glenn Mueller, head of Legg Mason's real estate research team. Several firms, including Salomon Smith Barney and EVEREN, say they plan to offer new REIT trusts as often as once a quarter as

long as demand holds up and REITs continue to need new financing.

Most of these trusts are made up of about 10 REITs, including those specializing in apartment, industrial, retail, and office buildings. To be in the trust, a REIT must work with the firm's investment banking division. That means the dealmakers have some role in the construction of the portfolio, although firms say the research department has the ultimate say in which REITs are chosen.

While you can buy shares of trusts already on the market, the real trick is to find out about upcoming offerings in time to get in during the no-load phase. So you need to know a broker at a firm

who can alert you, or call 800 numbers of potential sponsors to find out if a new real estate UIT is in the works.

Be aware that trusts are hard to research. You won't even know which REITs are included until the trust is priced. That could spell trouble if some of the REITs turn out to be a bust. Given a UIT structure, a trust can't dump problem holdings. Another

drawback: When trusts are liquidated, you may be forced to cash out even if you prefer to hold the trust as a long-term play. That may trigger a taxable gain.

BAILING OUT. To get some clue about the potential portfolio, ask your broker or financial adviser for a list of the firm's current and past REIT picks with their total returns. If you buy in and the real estate market turns south, you can always sell your UIT shares back to the firm which makes a market in the shares. Firms say there is no commission for redemptions and they buy back shares at their current market value.

An alternative to a REIT UIT is a real estate mutual fund. Nearly 50 such funds are available now, and more are cropping up. Two promising new ones are T. Rowe Price Real Estate and Cohen & Steers Special Equity, although both are down so far this year. In fact, the average real estate mutual fund has fallen 2% in 1998, according to Morningstar.

The advantage in owning REITs through a mutual fund is that you have a portfolio manager on hand to make adjustments if real estate market conditions change or better opportunities come along. UITs, on the other hand, appeal to investors who want to stick with a fixed portfolio and don't want to pay management fees or trade the portfolio. The way the REITs have been selling, there are plenty of those people around. *Amey Stoeck*

SMART MONEY



Who Offers REIT Trusts

FIRM	TRUST FORMED	DIVIDEND YIELD*	YEAR-TO-DATE RETURN*
SALOMON SMITH BARNEY	9/11/97	6.3%	-1.4%
LEGG MASON WOOD WALKER	12/18/97	6.0	-1.2
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When it comes to personal computers, life just isn't fair. Little more than

two weeks ago, I spent nearly \$2,000 for a middle-range 120-MHz Pentium. The machine is equipped with 16 megabytes of RAM, a 1.6-gigabyte hard drive, a decent sound card and speakers, and—my one splurge at the time—a Viewsonic monitor. I subsequently surrendered an extra 500 bucks to double the machine's memory, insert a second 5.1-gig hard drive, and add a speedy 56k modem.

Imagine my chagrin each time I peer at ads trumpeting multimedia hummers that cost \$1,000 or less. Indeed, by laying out not much more cash than I spent upgrading my current configuration, I could now cart home a brand-new PC system that, save for the monitor, outshines my 27-month-old in most respects. Spend a few hundred dollars more than that, and I'd own a true PC thoroughbred.

What's more, prices may go further south in the next few months with the introduction of Pentium machines that are based on Intel's new 486-compatible chips. These will compete with cheaper PCs that employ chips from AMD and Cyrix. Your end price could fall as low as \$600,

with bundles that include printers in the \$1,000 range. Even so, it's a terrific time to jump in now. We buyers have always lamented that our computers seemed out-dated almost from the moment we took them out of their boxes. The difference now is that where you once had to spend \$2,500 or more for the next greatest model, you can bring home a perfectly suitable PC for less than half the cost.

FAMILY PEACE. With memory and component prices falling dramatically, PC companies are building low-priced machines on purpose, rather than just holding fire sales on yesterday's models. Many people are purchasing these cheapie concoctions as a second or third computer to satisfy their spouses and kids who all want to use the computer at the same time.



COMPUTERS

The "subzero" that are all the rage pack enough power to give El Niño a run for its money. These machines come from Compaq, Hewlett-Packard, IBM, Packard Bell, NEC, and others among the usual suspects. Though giving no details, Apple is broadly hinting that

it too will have a sub-\$1,000 entry this fall. The current cheapie PCs run plenty fast enough for you to track the family budget, explore the Internet, or help the kids prepare school reports. On the business side, Gateway 2000, which has resisted entering the sub-\$1,000 consumer market, has unveiled a \$999 machine for corporate customers. Both home and business users once felt the urge to trade up every few years to run the latest operating system or compelling new software application. But there's nothing on the horizon, including Windows 95 that could tax the

sub-\$1,000 system's capabilities anytime soon. What people worry most about is being able to surf the Web at warp speeds, and even the cheapest PC systems packaged with the latest modems.

QUICK CHANGE. For the first time at home, a grand nowaday typically buys you a computer that carries a capable 100-MHz, Pentium MMX processor, a two-to-three-gig hard drive, and 32 megs of RAM. Some will do a lot better than that. For \$999, Acer's Aspire 2842 comes with a 100-MHz Pentium, 48 megs of RAM, and a generous 5.7-gig hard drive. Those state-of-the-art specs are a far cry from a year ago. (For a results on several sub-\$1,000 models, check out BUSINESS WEEK's Maven Web site at www.maven.bu.com.) The tests were conducted by National Software Test Laboratories, which, like BUSINESS WEEK, is owned by The McGraw-Hill Companies.

That's not to say that a \$1,000 should make it a

Companies are building low-priced machines on purpose rather than holding fire sales on last year's models

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Everyone's desktop. Plenty of PC diehards crave the speediest processors and a bigger hard drive—never a bad idea—and want to take full advantage of emerging technologies such as DVD, or digital video disk. You'll have to pay \$1,500 and on up for a machine that boasts such capabilities.

What's more, if you're into heavy-duty number-crunching or arcade-quality action games, the sub-\$1,000 machines, with their mediocre graphics capabilities, don't cut it. Many low-priced systems only come with one megabyte of video memory, so make sure you can add an extra megabyte without hassling. "It's not until you get into digital imaging, desktop publishing, and intensive multimedia gaming that you start driving the need for higher-end processors," says Alex Gruzen, product marketing manager for desktop PCs at Compaq.

Keep in mind that sub-\$1,000 price tags can be mis-

The Computer You Can Buy For...

...\$1,000

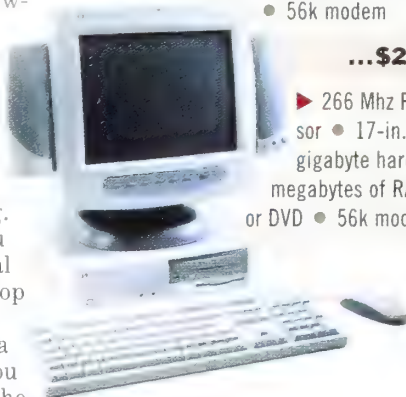
- ▶ 200 to 233 Mhz Pentium MMX processor • 14-in. monitor • 2-to-3-gigabyte hard drive • 32 megabytes of RAM • 16x to 20x CD-ROM • 56k modem

...\$1,500

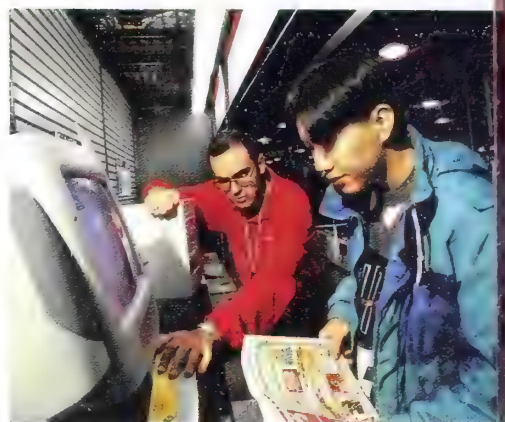
- ▶ 233 Mhz Pentium II processor • 15- to 17-in. monitor • 4-to-6-gigabyte hard drive • 32 to 48 megabytes of RAM • 24x CD-ROM • 56k modem

...\$2,000

- ▶ 266 Mhz Pentium II processor • 17-in. monitor • 6.4-gigabyte hard drive • 48 to 64 megabytes of RAM • 24x CD-ROM or DVD • 56k modem



leading. You'll usually have to fork over extra cash for a monitor. For example, adding a 14-in. monitor to the Acer Aspire 2842 would set you back \$225, pushing the total



UPGRADE? Be sure your machine takes add-on

price to four figures. A 17-in. Acer monitor costs \$449. Whichever system you are considering, you should choose the largest-size monitor that you

can afford.

Think also about whether you might want to upgrade somewhere down the road. Some of the sub-\$1,000 models offer only one or two available expansion bays and slots for adding, say, a 3-D graphics accelerator card or extra hard drive. HP's slim-line Pavilion 3260 model, for example, has no empty in-

ternal bays and just a few available slots.

As always, the choice lies with how you and the rest of the clan plan to use it. If you just intend to write a few letters or bring home a modest amount of work from the office, you can probably live with a system that takes a few seconds longer to complete those projects on Word or Excel. And even if you are a game devotee, you might find yourself whether spending extra grand to get the most out of them is worth the extra expense. For my money, these cheaper machines are just fine. *Edward C. Ba*

FUND WATCH

SIMPLE CREDO, FANCY RESULTS

Vanguard's Total Bond Market Portfolio aims to match the moves of the bond market while keeping costs low—much like its equity-fund cousin, the popular Vanguard Index 500. With nearly \$5.5 billion in assets, the fund has outperformed 82% of intermediate bond funds over the past three years, according to Morningstar. **BUSINESS WEEK** Senior Writer Robert Barker spoke with manager Kenneth Volpert:

Q: Why are you beating your rivals?

A: The average expense ratio in the group is... 106 basis points, vs. the fund, which is 20. [One basis point equals one hundredth of a percentage point.] So that's basically 85 basis

points of value added just from the expense ratio differential.

Q: Some active bond managers have steadily beaten the market. Why invest in a passive index fund rather than giving your money, say, to Pacific Investment Management Co.?

A: Well, if you feel pretty confident that [Pimco's high returns] will continue, O.K.... But historical performance is not a good predictor of future performance. That's not to say Pimco won't continue to do well. Obviously, it's an excellent shop... but there are relatively few of those shops that have been able to do it year in and year out.

Q: Want to run an active fund?



VOLPERT

A: No. I worked for an active manager from '81 to '86 and that drove me to the indexing business. I was dismayed with having so much of the bets driven by interest rates. What I started to believe in was multiple smaller bets. A lot of smaller bets. And for me, none of it is interest-rate related.

Q: Knowing bonds as you do, where's the biggest threat to investors?

A: Bonds of companies heavily involved in commodities from Asia or that make goods in competition with Asian companies I think are going to have a lot of pressure. Also, if our economy has a downturn, there's significant risk in high-yield [junk] bonds.

For an expanded version, go to www.businessweek.com/today.htm or AOL, keyword: BW Daily

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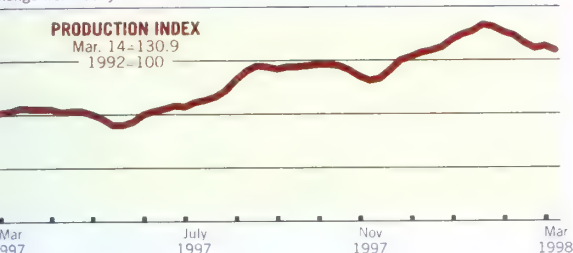
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PRODUCTION INDEX

Change from last week: -0.3%
Change from last year: 4.3%



The index is a 4-week moving average. The production index was down in the week ended Mar. 14. The unaveraged index also fell, to 130.9 from 131.3 in the previous week. After seasonal adjustment, the majority of the components were down. Severe winter storms in the Midwest caused the 9.1% decline in rail freight traffic. Coal production was up 14%, with the largest upsets in Colorado, Utah, Alabama, and Wyoming. Production of steel, trucks, oil, and lumber also dipped. Auto production was up and electric power was up 6.3%.

Production index: Copyright 1998 by The McGraw-Hill Companies

LEADING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STOCK PRICES (3/20) S&P 500	1099.16	1068.59	40.2
CORPORATE BOND YIELD, Aaa (3/20)	6.66%	6.69%	-12.5
INDUSTRIAL MATERIALS PRICES (3/20)	95.2	95.1	-11.5
VEHICLE SUPPLY, M2 (3/9) billions	\$4,117.7	\$4,114.4r	6.6
UNEMPLOYMENT (3/14) thous	308	299r	-1.9
MORTGAGE APPLICATIONS, PURCHASE (3/20)	234.1	217.2	18.7
MORTGAGE APPLICATIONS, REFINANCE (3/20)	1,421.4	1,337.9	258.3

Sources: Standard & Poor's, Moody's, Journal of Commerce (Index: 1990=100), Federal Reserve, Labor Dept., Mortgage Bankers Assn. (Index: March 16, 1990=100)

INTEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
MORTGAGE FUNDS (3/24)	5.41%	5.47%	5.57%
COMMERCIAL PAPER (3/24) 3-month	5.48	5.47	5.70
CERTIFICATES OF DEPOSIT (3/25) 3-month	5.58	5.58	5.66
FIXED RATE MORTGAGE (3/20) 30-year	7.15	7.22	8.09
ADJUSTABLE RATE MORTGAGE (3/20) one-year	5.76	5.86	5.85
LIBOR (3/20)	8.50	8.50	8.50

Sources: Federal Reserve, HSH Associates, Bloomberg Financial Markets

Data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

HOME SALES

Wednesday, Mar. 30, 10 a.m. EST ▶ New homes sold at an annual rate of 860,000 in February, says the median forecast of economists surveyed by Standard & Poor's MMS, The McGraw-Hill Companies. In January, 77,000 homes were sold.

MEETING

Monday, Mar. 31 ▶ The Federal Reserve's Market Committee will meet to set monetary policy. The S&P MMS economists expect no change in interest rates.

CONSUMER CONFIDENCE

Monday, Mar. 31, 10 a.m. EST ▶ The Conference Board's consumer confidence index

likely slipped to 137.2 in March after jumping 10 points in February, to a reading of 138.3.

NAPM SURVEY

Wednesday, Apr. 1, 10 a.m. EST ▶ The S&P MMS survey forecasts that the National Association of Purchasing Management's business index likely fell to 53% in March, from 53.3% in February.

CONSTRUCTION SPENDING

Wednesday, Apr. 1, 10 a.m. EST ▶ Construction spending probably rose 0.5% in February, as suggested by the jump in housing starts. Unseasonably warm weather helped lift outlays by 0.7% in January.

LEADING INDICATORS

Wednesday, Apr. 1, 10 a.m. EST ▶ The Conference Board's index of leading indicators probably rose 0.2% in February after no change in January.

FACTORY INVENTORIES

Thursday, Apr. 2, 10 a.m. EST ▶ Factory inventories likely fell a bit in February after increasing just 0.1% in January.

EMPLOYMENT

Friday, Apr. 3, 8:30 a.m. EST ▶ The S&P MMS median forecast expects that nonfarm payrolls rose by 235,000 in March, on top of February's huge 310,000 gain. The jobless rate likely remained at 4.6%.

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (3/21) thous. of net tons	2,250	2,102#	6.3
AUTOS (3/21) units	122,555	117,333#	-3.2
TRUCKS (3/21) units	147,862	137,583r#	12.7
ELECTRIC POWER (3/21) millions of kilowatt-hrs.	61,674	64,390#	3.9
CRUDE-OIL REFINING (3/21) thous. of bbl./day	11,734	14,581#	-16.7
COAL (3/14) thous. of net tons	20,171#	22,916	-6.5
LUMBER (3/14) millions of ft.	475.0#	477.8	-6.7
RAIL FREIGHT (3/14) billions of ton-miles	25.4#	27.5	-6.3

Sources: American Iron & Steel Institute, Ward's Automotive Reports, Edison Electric Institute, American Petroleum Institute, Energy Dept., WWPAI, SFPAP, Association of American Railroads

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (3/25) \$/troy oz.	299.250	290.400	-13.5
STEEL SCRAP (3/24) #1 heavy, \$/ton	135.50	135.50	-0.7
COPPER (3/20) ¢/lb.	83.8	84.1	-28.8
ALUMINUM (3/20) ¢/lb.	69.8	69.5	-12.7
COTTON (3/21) strict low middling 1-1/16 in., ¢/lb.	67.78	64.42	-4.0
OIL (3/24) \$/bbl.	15.40	12.99	-25.9
CRB FOODSTUFFS (3/24) 1967=100	230.47	229.73	-6.0
CRB RAW INDUSTRIALS (3/24) 1967=100	304.07	305.07	-10.4

Sources: London Wednesday final setting, Chicago market, Metals Week, Memphis market, NYMEX, Commodity Research Bureau

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (3/25)	129.06	130.22	124.23
GERMAN MARK (3/25)	1.83	1.83	1.69
BRITISH POUND (3/25)	1.67	1.67	1.63
FRENCH FRANC (3/25)	6.13	6.12	5.70
ITALIAN LIRA (3/25)	1800.0	1799.8	1685.5
CANADIAN DOLLAR (3/25)	1.41	1.42	1.37
MEXICAN PESO (3/25)	8.517	8.575	7.893
TRADE-WEIGHTED DOLLAR INDEX (3/25)	109.6	110.2	105.1

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars. Trade-weighted dollar via J.P. Morgan

This Week, Online

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Thursday

Buy, sell, or hold? Stocks, bonds, or mutual funds? Bounce your investment questions off BW Online's guest expert. **Apr. 2 9 p.m. EST in BW Online's Conference Room**

Enterprise

Update: BW Enterprise chats for small business and entrepreneurs are moving to a new day and time. Starting **Apr. 5, tune in on Sundays. 9 p.m. EDT in the BW Enterprise Chat Room**

B-Schools

Students from top business schools brief aspiring MBAs on campus life.

Mar. 31: Rochester

Apr. 2: Vanderbilt

8 p.m. EST in the

BW Online Chat Room

AOL keyword: BW Talk

Transcripts of all conferences are available for downloading from the BW Online area on AOL soon after each event.

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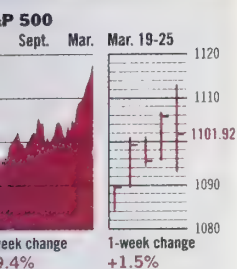
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STOCKS



MENTARY

stock market hit another bagger this week. The Dow Jones Industrial Average, the S&P 500 stock index, the NASDAQ composite, and the Russell 2000 index all reached new highs. Indeed, early in the trading day on Mar. 25, the Dow was booming ahead of the S&P 500 by 50 points shy of the 9000 mark, only to sell off a bit. Tech stocks were especially strong, propelled by Microsoft's announcement that earnings would exceed forecasts. A word of caution: The Vickers Put/Call ratio, a technical indicator shown on this page, is giving negative signals.

U.S. MARKETS

	Latest	% change Week	Year
Dow Jones Industrials	8872.8	1.1	29.0
NASDAQ Combined Composite	1824.5	2.0	43.8
S&P MidCap 400	368.5	1.0	41.0
S&P SmallCap 600	199.1	1.0	41.0
S&P SuperComposite 1500	236.1	1.4	39.6

SECTORS

	Latest	% change Week	Year
Bloomberg Information Age	338.5	3.7	42.8
S&P Financials	133.9	-0.2	47.4
S&P Utilities	247.9	2.3	28.1
PSE Technology	345.3	1.7	37.3

FOREIGN MARKETS

	Latest	% change Week	Year
London (FT-SE 100)	5967.8	1.1	38.7
Frankfurt (DAX)	5096.6	3.6	49.1
Tokyo (NIKKEI 225)	16,658.3	0.2	-9.8
Hong Kong (Hang Seng)	11,810.6	6.2	-7.6
Toronto (TSE 300)	7579.2	2.1	23.8
Mexico City (IPC)	4997.1	3.2	30.0

FUNDAMENTALS

	Latest	Week ago	Year ago
S&P 500 Dividend Yield	1.36%	1.43%	1.86%
S&P 500 P/E Ratio (Last 12 mos.)	27.7	27.1	20.7
S&P 500 P/E Ratio (Next 12 mos.)*	21.9	21.3	16.6
First Call Earnings Revision*	-3.48%	-3.51%	-0.99%

TECHNICAL INDICATORS

	Latest	Week ago	Reading
S&P 500 200-day average	957.4	951.2	Positive
Stocks above 200-day average	67.0%	66.0%	Neutral
Options: Put/call ratio	0.58	0.54	Negative
Insiders: Vickers Sell/buy ratio	2.52	2.01	Negative

Data: Bloomberg Financial Markets; *First Call Corp.

BEST-PERFORMING GROUPS

	Last month %	Last 12 months %
Steel	15.7	Homebuilding 94.1
Pollution Control	14.7	Broadcasting 93.8
Savings & Loans	14.0	Manufactured Housing 88.1
Hospital Management	13.8	Communications Equip. 84.0
Hotels & Motels	13.3	Specialty Appar. Retailers 80.9

WORST-PERFORMING GROUPS

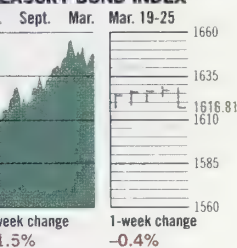
	Last month %	Last 12 months %
Semiconductors	-14.3	Shoes -32.7
Drug Chains	-3.8	Metals -31.8
Toys	-3.2	Gold Mining -28.9
Computer Systems	-2.8	Photography/Imaging -13.7
Transportation Services	-2.7	Engineering & Constr. -10.4

BLOOMBERG MONEY FLOW ANALYSIS

Rebound ahead? Stocks with most significant buying on price weakness	Price	1-month change
IBM	103 1/2	-1 3/4
Micron Technology	28 11/16	-6 7/16
Compaq Computer	25 9/16	-8 7/16
Sun Microsystems	44 7/8	-1 9/16
Ascend Communications	34 13/16	-1 7/16
Texas Instruments	53 5/16	-7 15/16
Decline ahead? Stocks with most significant selling on price strength	Price	1-month change
Dell Computer	65 3/4	25/32
WorldCom	44 7/16	6
Cisco Systems	67 13/16	1 1/16
Pfizer	95 3/8	7
PeopleSoft	50 7/8	6 7/8
Qwest Communications Intl.	39 3/4	3 1/2

INTEREST RATES

TREASURY BOND INDEX



Bloomberg Financial Markets

KEY RATES

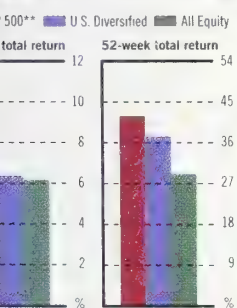
	Latest week%	Week ago%	Year ago%
MONEY MARKET FUNDS	5.11	5.12	4.96
90-DAY TREASURY BILLS	5.17	5.17	5.44
6-MONTH BANK CDS	5.07	5.07	5.07
1-YEAR TREASURY BILLS	5.37	5.36	5.91
10-YEAR TREASURY NOTES	5.64	5.58	6.75
30-YEAR TREASURY BONDS	5.94	5.91	6.95
LONG-TERM AA INDUSTRIALS	6.51	6.48	7.45
LONG-TERM BBB INDUSTRIALS	6.98	6.95	7.79
LONG-TERM AA TELEPHONES	6.79	6.78	7.65

BLOOMBERG MUNI YIELD EQUIVALENTS

Taxable equivalent yields on AAA-rated, tax-exempt municipal bonds, assuming a 31% federal tax rate.

	10-yr. bond Latest week	Last week	30-yr. bond Latest week	Last week
GENERAL OBLIGATIONS	4.43%	4.42%	5.03%	5.02%
PERCENT OF TREASURIES	78.54	79.36	84.64	85.02
TAXABLE EQUIVALENT	6.42	6.41	7.29	7.28
INSURED REVENUE BONDS	4.57	4.54	5.21	5.18
PERCENT OF TREASURIES	81.02	81.51	87.67	87.73
TAXABLE EQUIVALENT	6.62	6.58	7.55	7.51

MUTUAL FUNDS



Morningstar, Inc.

EQUITY FUNDS

Leaders	Laggards
Four-week total return %	Four-week total return %
Amerindo Technology D 18.2	ProFunds UltraBear Svc. -12.6
Fidelity Sel. Energy Serv. 16.8	Frontier Equity -8.3
Smith Barney Telecom. Income 16.6	Merrill Technology D -6.9
Matthews Korea I 14.4	Rydex Urss -6.5
Weitz Hickory 14.4	Warburg Japan OTC Comm. -5.8
Leaders	Laggards
52-week total return %	52-week total return %
Delaware Aggressive Gr. A 98.8	Midas -58.5
Munder Micro-Cap Equity Y 84.8	U.S. Global Investors Gold -57.5
FMI Focus 79.5	Invesco Strategic Gold -54.5
Fidelity Select Brokerage 73.7	Bull & Bear Gold Investors -53.8
Safeco Growth No Load 72.9	Gabelli Gold -48.8

EQUITY FUND CATEGORIES

Leaders	Laggards
Four-week total return %	Four-week total return %
Communications 11.3	Japan -2.1
Latin America 9.8	Real Estate 0.0
Europe 9.2	Diversified Pacific/Asia 1.6
Utilities 8.7	Technology 2.4
Foreign 7.6	International Hybrid 4.0
Leaders	Laggards
52-week total return %	52-week total return %
Communications 57.4	Precious Metals -38.5
Financial 48.8	Pacific/Asia ex-Japan -30.1
Large-cap Growth 41.6	Diversified Pacific/Asia -22.1
Small-cap Blend 40.1	Japan -9.4
Unaligned 39.2	Diversified Emerging Mkts. -7.3

are as of market close Wednesday, Mar. 25, 1998, unless otherwise indicated. Industry include S&P 500 companies only. Fundamentals, technical indicators, Bloomberg mon-

ey flow analysis, and mutual fund returns are as of Mar. 24. For a more detailed explanation, write to us or E-mail figures@businessweek.com. NA=Not available **Vanguard Index 500 Fund

LET'S NOT RUSH TO TAX THE NET

Everyone hates taxes—especially when they're imposed where they didn't exist before. That's why the debate over taxing the Internet is so heated. Governors want to extend state sales taxes to the burgeoning business taking place on the Net. Electronic-commerce merchants and some in Congress say "forget about it." A better response is "Cool it." It's time to shed some light, as opposed to heat, on the issue.

It's true that governors rely increasingly on sales taxes to fund schools, pay salaries, and repair roads. They don't want to lose revenues if business shifts to a tax-free Net. Fair enough. But states are running budget surpluses now, thanks to the strong economy. In fact, most governors are rushing to cut taxes. There's no immediate need to tax the Net.

The Net is not the first no-tax zone. Mail-order retailers have been thriving for decades. The Supreme Court's decree that only companies with a physical presence in a state are required to collect sales taxes there has helped catalog sales soar to \$78 billion in 1997. Compare that with \$4 billion in electronic commerce. If mail order isn't threatening state solvency today, the Net probably won't anytime soon (page 131).

Then there's the matter of tax policy. Government has tended in recent years to shift revenue sources from income, property, estate, and capital-gains taxes to sales and payroll taxes, which are regressive. Some three-quarters of all households now pay more in payroll taxes than in income taxes. Sales taxes have the virtue of being simple and transparent—everyone pays them equally. But they do fall more heavily on the poor than the rich, and they must be paid in good times as well as in bad. They are also a heavy burden—8% in New York, which helps explain why people like catalog shopping.

Extending a regressive tax to the Net is a bad idea. Any discussion of Net levies should be part of a larger debate over simplifying and broadening taxes, making them both fairer and lighter. The Net is too young an arena and too important to the nation's competitiveness to tax just because it's there.

THE LOWEST-PAID GET A BREAK AT LAST

Wages for the lowest-paid workers in the U.S. rose 1.6% in 1997, nearly twice as fast as wages for the best-paid. That's the biggest increase in inflation-adjusted pay since the government started collecting data in 1979. Economic growth is benefiting workers on the bottom half more than those on the top half. Is this a fluke? What about all those immigrants willing to work for less? How about all those jobs going offshore, thanks to the huge trade deficit?

The new economy continues to surprise. The largest blemish of this expansion had been a growing inequality in pay.

But with unemployment down to 4.6%, labor markets tight enough to support higher weekly earnings for the bottom 10% of the pay scale. Whatever downward pressures the global economy is putting on wages, fast economic growth (3.8% last year) and labor scarcity are more than compensating for it. This is particularly good news for unskilled young people entering the job market. The jobless rate for high school dropouts is down from nearly 12% in 1992 to 7%.

Judicious use of government policy has helped. The Earned Income Tax Credit amplifies the gains in disposable income for the working poor. And the hike in the federal minimum wage, in a period of low unemployment, boosts earnings.

The weekly earnings figures probably measure only a portion of the real gains made recently at the bottom half. They do not measure mobility—and with fast growth, low inflation, and tight labor conditions, our guess is that Americans are taking the upward-mobility escalator more than ever. Growth is good. Strong, noninflationary growth is better.

A SIMPLE FIX FOR PENSION SAVINGS

Political battle lines are being drawn on how best to save Social Security. President Clinton wants to use the federal budget surplus. Conservatives want privatization. Liberals want to hike payroll taxes. Senator Daniel Patrick Moynihan (D-N. Y.) supports partly privatizing Social Security. Others believe higher economic growth will do the trick. But any consensus will take time to form. Meanwhile, Congress can do something right away to ease the retirement worries of millions of people working in the New Economy: simplify, and don't penalize mobility.

In a high-tech global economy, job loss and job creation go together. People shift jobs to different sectors all the time. America's retirement-savings system is balkanized. There are 401(k)s for the private sector, 403(b)s for nonprofits, 457s for state- and local-government employees, Keoghs and Simplified Employee Pension Individual Retirement Accounts for self-employed, and IRAs and Roth IRAs for those who qualify.

This results in a tangle of different rules, income limits, and restrictions. If you're a state trooper, you can't roll over a 401(k) into an IRA when you leave your job. But you can if you're a business manager with a 401(k). If a corporate lifer decides to change careers and teach at a university, the ex-exec's 401(k) pension can't be transferred into a 403(b). Married couples with an adjusted gross income of up to \$150,000 can contribute as much as \$2,000 to a Roth IRA. But to set up a traditional IRA, the income limit is \$50,000 if they are covered by a retirement plan. Go figure.

Why not just let everyone save, tax-free, 15% of their income or \$10,000, which is close to the maximum contribution for a 401(k) plan? Indeed, with budget surpluses soaring, why not let people save even more? It's time for Congress to streamline the retirement savings system to reflect the realities of the new economy. Do it now.



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THE
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COVER STORY

THE EDUCATION OF ANDREESSEN

You wouldn't think a kid who once was worth \$170 million would have much to learn. Guess again

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Cover Story

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Having helped found a company whose fortunes have risen and fallen dramatically, he has already had a roller-coaster ride of a life. Now it's about to get much more interesting. Andreessen is stepping into a fresh role: Developing products for Netscape as it fights off big, hungry Microsoft. Can a 26-year-old techie *wunderkind* prosper in an increasingly corporate career?

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THE GERMANS ROAR

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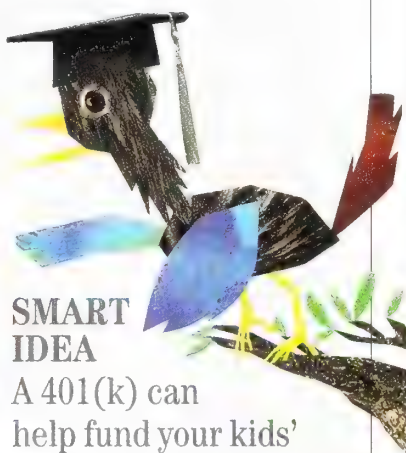


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Up Front

EDITED BY ROBERT McNATT

FED WATCH

O. K., GREENSPAN, YOU WIN

ALAN GREENSPAN MAY NOT walk the halls of the Federal Reserve telling his fellow central bankers, "I told you so." But they are gradually accepting the Fed chairman's view that productivity gains really are taming inflation.

Up to now, other Fed policymakers did not fully share Greenspan's belief that heavy corporate spending on computers and other technology was fueling a productivity boom. Vice-Chair Alice Rivlin, for one, said last year that she remained puzzled why robust growth had not triggered a



RIVLIN: Leaning

rise in inflation. But in March, Rivlin said she's more confident that productivity is key. And Fed Governor Laurence Meyer, one of the leading skeptics, recently told some outside economists that his estimate for long-term productivity growth is now 1.4%, not 1.1%. Fed Governor Edward Gramlich is also known to have raised his estimates.

The central bank's growing optimism about productivity could give the Fed the resolve to hold off firing a preemptive strike against inflation, says Fed-watcher James Annable, chief economist for First Chicago NBD. Now, the Fed may wait until prices rise before raising rates.

Dean Foust

REGULATION NATION

RED TAPE AND ROBBERS AT THE MINIMART



FREEZE: Convenience store arrest

LAST YEAR, DOZENS OF employees lose their lives during robberies at retail outlets. So asking for pumped-up security measures at convenience stores seems like a no-brainer.

It's not. The Occupational Safety & Health Administration wants to set voluntary guidelines this month, which would ask for bulletproof glass and two clerks on late-night shifts in convenience stores. Bitterly opposing the

rules is the convenience store industry, which says OSHA is unfairly singling it out.

So why the flap over something voluntary? Says crime consultant Rosemary Erickson of San Diego: "If these guidelines go through, they could also be enforced under existing regulations, and we are concerned about the litigation factor." In other words, the industry fears "voluntary" will end up meaning "mandatory."

Southland, the owner of 7-Eleven Stores, says it has managed to reduce robberies 64% in the past 20 years without OSHA's interference. So expect a regulatory shoot-out when OSHA issues final guidelines later this month. The industry says it may then take the fight to Congress.

Dennis Blank

TALK SHOW "As Woody Allen said in *Bananas*, 'It's a travesty of a mockery of a sham.'"

—Representative Martin Meehan (D-Mass.) after the House Republican leadership killed the campaign-finance reform bill

TRENDLETS

BEST MEDICINE I EVER ATE

THEY MAY TURN OUT TO BE the ultimate health foods. They're pharmafoods, or nutraceuticals—everyday grub that has been chemically or genetically engineered to fight specific health problems. Cleveland researcher Freedonia Group says the market for health-food additives and pharmafoods may be \$2.5 billion in 2001.

Monsanto, for one, is developing a cholesterol-lowering corn sugar and a strain of rice that provides insulin. They aren't expected to be ready before 2000. But Nestlé already makes a yogurt in Europe, Yacult, that supposedly boosts the immune system.

Finland's Raisio Group has hooked up with McNeil Consumer Products to launch a cholesterol-cutting margarine called Benecol in the U.S. this fall. Benecol, now on sale in Europe, was developed from a

byproduct of pulp paper production. Sound unpalatable. Maybe. But analysts are savoring over its prospects. After its U.S. launch, global sales could hit \$400 million.

There may be regulatory problems, however. Dire claims of health benefits will



require an O.K. from the Food & Drug Administration. Benecol still does not have a firm U.S. marketing strategy. But ultimately, pharmafoods could be a way to have our cake and eat healthfully, too.

William Echikson

REALITY CHECKS

AT&T'S FALLEN ANGEL

JUST OVER A YEAR AGO, AT&T announced Project Angel, a new phone technology designed to break the Baby Bells' death grip on local phone service. Trumpeting Project Angel as "revolutionary," AT&T said it would offer consumers local calls and high-speed Internet connections, all while bypassing local phone companies.

Now, AT&T's Angel dream has met up with reality. In a meeting with BUSINESS WEEK, CEO C. Michael Armstrong revealed that the cost of deploying the



ARMSTRONG

technology is \$1,100 per home on average. That is double the price at which AT&T can turn a profit, he said.

The Angel system uses radio technology to bypass the wires of local phone companies. AT&T still plans to expand the small Angel test that's currently underway in Chicago. Armstrong estimates that Angel's cost eventually will drop to \$50 per household, a price that should make it profitable. "It's a matter of time," he says. "It'll probably take two more cycles of technology." That

means it will be several more years before AT&T's Angel can compete in the \$100 billion local phone market.

Peter Elstrom



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FASHION STATEMENTS

MUNSINGWEAR WILL TAKE THIS RAP

WHAT DO HIP-HOP STAR PUFF Daddy and crooner Bing Crosby have in common? Their shirts, of course.

Munsingwear, makers of the knit golf shirts once favored by Crosby, is scoring big with a revamped line of the shirts. With their penguin logo, the company's \$40 Grand Slam and Grand Slam Tour shirts have become must-wears for the hip-hop set. Result? Miami-based Supreme International, the label's owner, has seen sales of the brand, including licensed products and other lines, grow to \$175 million from \$30 million last year. Puff Daddy, born Sean



ALL PENGUIN: *Daddy*

Combs, sports the shirts in his recent video, *Mo Money Mo Problemz*, though he isn't paid to endorse them. Says Katina Masouras, an assistant producer at MTV, the "old-school" style has always appealed to rappers. Once, for instance, Izod rode that high.

Munsingwear also benefits from the golf craze among African Americans spurred by Tiger Woods. One of its print ads shows a black golfer with the tagline: "The best golfers wear the penguin until they are paid not to." It's a tongue-in-cheek reference to Woods, who wore Munsingwear before signing with Nike. The company estimates only 30% of its shirts are worn by golfers. The other buyers? They just like the look. *Christina Scott*

SLUGFESTS

THEY'RE BOILING OVER RICE

IT'S BECOMING THE GREAT Basmati Scandal. RiceTec Inc., a rice producer in Alvin, Tex., has received a U.S. patent for a new strain of basmati rice. It wants to use the name in conjunction with its Texmati, Kasmati, and Jasmati brands. All are Texas-grown versions of basmati rice, which originated in the foothills of the Himalayas.

U.S. basmati? Indians are steamed at the thought. In India, after all, medieval poets have written odes to the aromatic rice. "They are

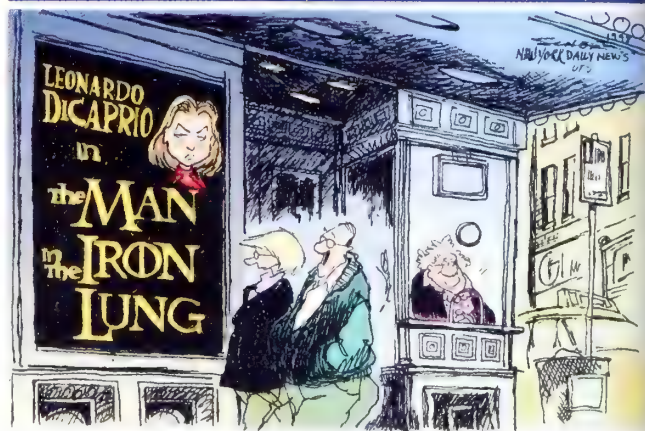
stealing our heritage," says Anil Adlakha of the All India Rice Exporters Assn. "America had not come into existence when our ancestors were growing basmati."

It's not just India's culinary heritage at issue. Big money is also involved. Indian farmers export \$250 million worth of basmati annually, and the U.S. is a target market.

RiceTec CEO Robin Andrews says that while the basmati name will be on the boxes, he's not trying to stop Indian exports. But India's Commerce Ministry is researching a challenge to the patent. This curry could simmer for a while. *Manjeet Kripalani*



DRAWN & QUARTERED



"LOOKS LIKE ANOTHER ATTEMPT BY BIG TOBACCO TO ATTRACT THE YOUTH MARKET."

STRAIGHT DOPE

IF A HIGH HAD A HIGHER PRICE

IF YOU WANT TO STOP teens from using cocaine, says a new economic study, think high prices. Youthful drug abusers are three times as sensitive to prices as adults are. So forcing street prices upward by cracking down on dealers is a good way to keep kids on the straight and narrow, the authors say.

The study contradicts earlier research that supported relaxing laws against cocaine and marijuana. Those studies said that prices don't affect usage much, so it wouldn't matter if decriminalization lowered the cost of drugs.

Authors Frank Chaloupka and John Tauras of the University of Illinois at Chicago and Michael Grossman of the City University of New York



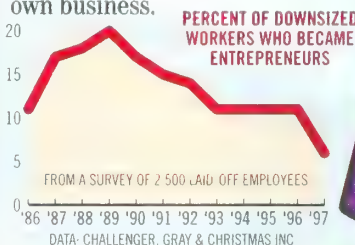
COKE: *What will teens pay?*

Graduate School found that a 10% increase in the price of cocaine reduces the chance of a youth's using the drug by 9% to 10%. They didn't have enough data to detect a similar pattern for marijuana. Unlike most other studies done on the subject, the authors had access to data from the Drug Enforcement Administration on the street price of cocaine. *Peter Coy*

THE BIG PICTURE

GIVE ME THE CORPORATE LIFE

The downsizing era that began in the late 1980s pushed a lot of folks into becoming entrepreneurs. With more jobs opening up in big corporations, though, people aren't as quick to start their own business.



FOOTNOTES A sizeable impact of high-tech on productivity, in poll: E-mail, 64%; spreadsheets, 62%; Internet, 19%

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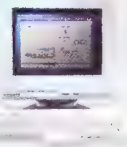


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just lose that market share, they
it away.

Robert H. Nielsen
Seattle

probable cause for GM's loss of
t share: design. Many of the GM
ts are just plain boring! Over
ears, I purchased three Buicks
nally gave up in disgust. They
e bland, adjusted to the lowest
on denominator of design.

might prove helpful if GM execu-
et the design departments have
flexibility and not approve de-
py committee. For starters, they
consider why the Corvette is a
nt best-seller!

William L. R. Rice
Fairfax, Va.

MAN'S LIGHT OUT YET

ough there are plenty of cost re-
n opportunities at Coleman Co.
nsaw Al goes to camp," News:
is & Commentary, Mar. 16), this
where the value lies. The real
of the acquisition will come from
g distribution and Coleman's
leadership position. Under Mike
es, Coleman perhaps focused too
on growth overseas and under-
ted the serious problems at home.
es with the Powermate Div. and
sources consumed in acquiring
egrating France's (not Germany's)
ng Gaz distracted management
ixing the problems in its core
outdoor business.

Hammes did not take the Cole-
name down-market. Sunbeam
t a great brand. It needs great
products. Al Dunlap's vision of
g a global consumer durable pow-
e with leading brands is similar to
sion that we had at Coleman in
still believe bringing this vision
ition will create tremendous
for shareholders.

David Yuen
Former Senior Vice-President
Coleman Co.
Hong Kong

NG A DOOR E PORTALS DEAL

spokesman for Franklin L.
I want to clear up two misim-
ns left by "The heat under Peter
." (Government, Mar. 16). First,
ing the \$1 million payment to
S. Knight's law firm for strategic
counsel: Knight worked on a
projects, including the Portals.
rticle implies that this payment
contingency fee and points out

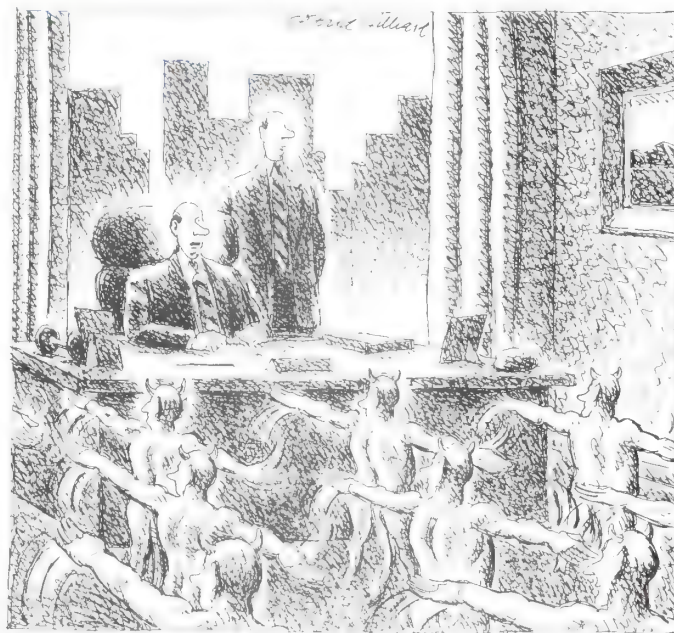
that the Portals' supplemental lease
had the same date as Knight's invoice
to developer Haney. How does the co-
incidence of these dates prove other-
wise? Haney would have owed Knight
his fee even if the Portals deal had not
closed.

Second, the article says that one of
Knight's main services was to secure a
fixed date for the Federal Communica-
tions Commission's rent payments to
begin at the Portals. A date was one of
a number of items negotiated by Portals

lawyers in exchange for millions in delay
damages the government could have
faced. Setting a date provided more fa-
vorable interest rates and better rental
fees for the government. The fixed date
meant that if the Portals developers'
failure to complete the project in time
were their fault, the government would
have gotten a full refund because of a
liquidated-damages provision.

As you reported, the building stands
empty, but the General Accounting Of-
fice made it clear that's not because of

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Readers Report

Haney. The GAO also says that the Portals is the best and most cost-efficient deal for the FCC. By the time the FCC moves in this summer, taxpayers will have lost \$14 million. It's time Congress, BUSINESS WEEK, and the FCC began focusing on that instead of searching through the long, sad history of this project for conspiracies that don't exist.

Kenneth Vest
Powell Tate
Washington

MARKETERS FEAR PRIVACY INVASIONS, TOO

Contrary to your recent article "A little privacy, please" (Information Technology, Mar. 16), progress in posting privacy policies is accelerating rapidly. Smart marketers know they will build better relationships with consumers by telling them how their personal information will be used, and more businesses are creating privacy policies at Web sites every day. Companies can get help in creating an online privacy policy at www.the-dma.org/policy.html. As your story noted, more than 700 organizations have posted policies after consulting the tool.

In no other medium has a self-regulatory code of conduct developed so fast to address consumer concerns. As E-commerce continues to evolve, companies are reacting quickly to determine the right set of actions to meet changing consumer demands.

H. Robert Wientzen
President & CEO
Direct Marketing Assn.
New York

FIRST UNION BANK'S SECOND-CLASS CUSTOMERS

In "Fast Eddie's future bank" (Finance, Mar. 23), Edward E. Crutchfield Jr.'s plans seem to have overlooked the consumer, like myself, who has seen the degradation of the local banking services after the takeover of First Federal in New Jersey. Since that time, I have seen a marked reduction in service accompanied by some of the highest fees in the country. First Union Corp. is now discouraging mail-banking by no longer supplying return-address envelopes and ceasing to confirm mailed deposits.

There is no doubt that First Union will continue on its profitable path. I can only ask why it has not received the attention of federal banking regulators.

Marvin G. Frank
Short Hills, N.J.

THE DIAMONDBACKS RATTLED A FEW ARIZONANS

In "Pitching 100 mph in Phoenix" (Sports Business, Mar. 30), you refer to Jerry Colangelo as "the man who brought Major League Baseball to the desert." What is not mentioned is that Colangelo did so on the backs of the taxpayers of Maricopa County. With certain members of the County Board of Supervisors as porters, and Colangelo as the train's engineer, unwilling citizens of the Valley of the Sun were transported—by rail—directly to the Stadium Tax Station. There were no stops along the way at any voting booths.

The Arizona Diamondbacks will play to sell-out crowds because there is an abundance of people in this valley whose only identity is the one printed on a T-shirt or ball cap. There are others who will show up at the new stadium on the day Phoenix has its first blizzard.

Harold Debbi
Scottsdale, Ariz.

THE MYTHICAL AMERICAN HIGH-TECH DUMMY

"High-tech talent: Don't bolt the golden door" (News: Analysis & Commentary, Mar. 16) is misleading. Studies show there is no shortage of indigenous high-tech talent. The industry's plea for a greater number of H-1B visas for immigrant workers is driven by the desire to hire the skills they need at the lowest possible cost. This is done with the expectation that as technology changes, today's immigrant tech talent will be let go to import another round of low-cost help.

The country has an ample supply of experienced indigenous computer specialists who can learn the newest technology in a short time. Of course, these midcareer professionals cannot, and should not, be expected to work at beginning wages. It does the country a great disservice to unnecessarily force it to rely on foreign workers for critical skills. As with any other profession, lifelong careers must be based on continuing education that adds to the value of experienced personnel.

John R. Thomas
Lafayette, Calif.

BEETLEMANIA IS ALIVE AND WELL

Yesterday, I experienced excitement, energy, and unbelievable euphoria—even nostalgia as I drove my new 1998 Volkswagen Beetle from Berkeley, Calif., to my home in Pleasanton ("The nostalgia

boom," Cover Story, Mar. 23). Yes, waved, pointed my fingers (peace, No. O.K.) toward every wave and smile that came my direction. Yes, the dealer even placed a daisy in the flower vase.

After all, I was one of the first to become a lucky owner of this vehicle. True, I owned a Beetle and just about every other vehicle VW has built over the years. My husband thought I had lost my marbles when I told him I had placed an order for the new Beetle. This was until yesterday, when he conceded the practicality of my decision. This car will be used for commuting, shopping, kid shuttle, and moving computer equipment and gardening supplies. This car will have many of the same uses a sport-utility vehicle performs today, offering better gas mileage and low cost. Today, I'm feeling groovy...

Dawn Pete
Pleasanton, Cal

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INVESCO

THE BIOTECH CENTURY

Harnessing the Gene and Remaking the World

By Jeremy Rifkin

Tarcher/Putnam • 271pp • \$24.95

TAKING ON THE GENE TINKERERS

For more than two decades, Washington activist Jeremy Rifkin has been practicing vigilantism in pursuit of biotechnology. As the industry has sped ahead at lightning pace, ostensibly for the public good, Rifkin has lurked around every bend, ready to challenge and spread fear and uncertainty about virtually any research on the manipulation of human genes. He has filed many lawsuits. He has enlisted some of the country's most prominent religious leaders to oppose patents on genes used to make drugs. And he has written a slew of books, such as *Declaration of a Heretic* and *Who Should Play God?*, attacking biotechnologists as greedy, arrogant Dr. Frankensteins. Rifkin argues that they are mortgaging public safety, our humanity, and the natural order for short-term profits.

I can sympathize with executives who turn crimson at the mention of Rifkin's name, but I've interviewed him enough to respect his intelligence and his sensitivity to notions that really freak people out—a sensitivity often much greater than exists in the industry. Give the guy credit: He knows how to get people's attention. When food companies paraded out experts to argue that gene-spliced foods were safe, for example, Rifkin matched them with a group of famous chefs who said: "Hey, we've got plenty of good, safe food now. Why even take a small risk?"

Rifkin's new book, *The Biotech Century*, was likely inspired by the recent fuss over Dolly, the cloned sheep. Indeed, he cribbed the book's title from a BUSINESS WEEK cover story also marking Dolly's arrival and the attendant opportunities, challenges, and ethical issues. "The new genetic technologies grant us a godlike power to select the biological futures and features of the many beings who come after us—the greatest shopping experience of all

time," Rifkin proclaims. True enough. And he fully explores his thesis that biotechnology and information science are converging, aiding the practice of what he dubs the "algenic" arts, or the "improvement" of living organisms. Genetic engineers are increasingly treating human DNA as they would a piece of software code, Rifkin notes, and society will confront unprecedented dilemmas. Just one: Fixing the genetic profiles of unborn children. Will insurance companies some day step in and mandate that parents take steps such as repairing the genes of potentially retarded children in order to save health-care dollars?

As usual, Rifkin asks important, provocative questions, but he muddies the discussion with a lot of scattershot industry-bashing. His anti-genetic-engineering rhetoric has mellowed a bit, but what Rifkin offers as alternatives to our current course of pretty much taking these issues as they come constitutes little more than a tower of unproductive bio-babble. *The Biotech Century* is ultimately a hand-wringing exercise that calls for "a rich and robust conversation" in society at large about a complex, technical, and, frankly, unstoppable field of inquiry.

To give Rifkin his due, he covers many serious issues that biotech raises and that the industry typically ducks. Among them: Who gets "authority to decide what is a good gene that should be added to the gene pool and what is a bad gene that should be eliminated?" It has been less than 100 years since respected American academics and politicians called for a ban on procreation by "inferior" people. Thus, it is troubling to contemplate what society might do as researchers expand their ability to find

and correct gene-based "defects." Everyone has some bad genetic baggage, Rifkin says, so we could "come to see ourselves as miswired from the get-go, riddled with errors in our code."

While there certainly are risks in monkeying around with genetics, much of that research is aimed at such goals as ending suffering, saving dying kids, and stopping infectious disease. In *The Biotech Century*, Rifkin is careful not to directly attack specific medical research projects, saving most of his fire for agricultural applications that he claims could unleash environmental havoc. He clearly recognizes that if he casts the debate in such a way that patient-advocacy groups or even the parents of a single suffering child take him on, he loses.

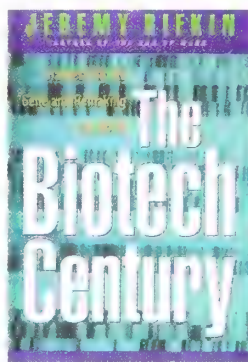
But Rifkin sees all corporations as profiteers and treats most of their experimentation with suspicion, attacking, for example, their alleged exploitation of Third World genetic resources, such as the "biopiracy" of medically beneficial genes from plants or animals. He weakly admits that many genetic-engineering projects could be beneficial but says we should explore other options first, such as studying environmental causes of illnesses. Does this mean we should shut down cutting-edge medical research until we know? That's unthinkable. And if not companies, who will develop new therapies?

With all new technologies, we need to consider the big picture and contemplate long-term consequences. But we can't slam every new development just because it goes against the natural order: So do antibiotics. So does bypass surgery. So do irrigation projects. So do airplanes.

Wail away, Jeremy, but if you or someone close to you ever gets sick and needs one of these gene-spliced drugs—or worse, suffers an untreatable illness—you may find yourself eating your words. In the end, one of biotechnology's most compelling aspects is its appeal to an awesome natural force: hope.

BY JOAN O'C. HAMILTON

Ex-bureau chief Hamilton covered biotechnology and now edits Signals, a Web magazine on biotechnology.



RIFKIN ASKS THE TOUGH QUESTIONS, BUT HIS SCATTERSHOT STYLE WORKS AGAINST HIM

STEPHEN H. WILDSTROM

DON'T BE CRASH DUMMY

Whether your
computer will go
down, it's when. Here
how to prepare

One morning a couple of weeks back, my hard drive started making funny clicking noises. I waited for a few more minutes with the computer flakier and flakier, then I panicked. An attempt to shut it down revealed the unsurprising awful truth. The disk had crashed. Nothing I could do would even reformatting, bringing it back to life. I could have been a disaster. My entire working life in columns that I've written, correspondence, E-mail addresses, expense reports, everything—was on a 2-gigabyte disk. To my great relief, it turned out nothing worse than a minor nuisance. Perhaps I can learn something from this experience.

LESSONS. If you use a computer, the question is not whether you will suffer a data loss due to hardware or software failure, but how I have endured several hard-drive crashes, which have taught me—the hard way in some cases—that preparation is all that stands between a computer catastrophe.

At this time, as soon as my hard drive went south, I made two phone calls. The first was to Connected, an on-line service to whose servers my data are backed up each month for a modest fee. The second was to Compaq Computer (since my Deskpro was in warranty). Each

promised relief by overnight delivery.

The next morning, I had two vital disks in hand. One was a replacement hard drive with Windows NT Workstation 4.0 already loaded. The other was a CD-ROM containing my file backups and the software needed to transfer them to the new hard drive. I still had several hours' work ahead of me, but by the end of the day, I was back in business.

Unless you have been singing a time or two, like I have, disaster recovery is probably the most overlooked piece of managing your computer. At best, most people will make floppy disk copies of some critical data files—when they think of it.

This is better than nothing, but it's nowhere near good enough. First of all, backup is something you want to have happen at regular intervals, whether you remember to do it or not. Furthermore, you're likely to overlook some critical data files. You might make copies of all your word-processing documents and spreadsheets but forget about your contact-manager database or last year's tax return. Furthermore, if you have spent any amount of time tweaking your applications to customize them, you're going to

lose all of those preferences.

The first piece of successful backup planning is software smart enough to understand what files need to be copied. You generally don't want to make copies of the programs themselves, partly because copying takes up a lot of time and storage space, and partly because the design of Windows requires that programs be reinstalled on, not just copied to, a new or reformatted disk. Good software also can be useful for reference by saving successive versions of files with the same name and different dates.

On-line backup, like that

restoring data. My only regret is that I should have been more careful in double-checking the list of files backed up: I lost some fonts and customized Microsoft Word templates.

BACKING UP. If you prefer to do your backups on your own machine, you'll have to spend \$100 to \$600 on a tape drive, a removable hard drive, such as Imega Jaz or SyQuest SparQ, or a writable CD. (Zip and LS-120 SuperDisks don't have enough capacity for convenient backup.) Some units, especially the tape drives, come with backup software. If you want

software that gives sophisticated control over the contents and scheduling of backups, I recommend Backup Exec from Seagate Software (800 327-2232 or 407 531-7501), which comes in a variety of versions for different systems, starting at about \$60.

In addition to up-to-date backups, you will also need the application CD-ROMs or floppies on hand. You need to have them all neatly gathered in one place. But if you're like me, you aren't quite that well organized. (If anyone knows where I put my WinFax Pro CD, let me know.) Do yourself a favor and hunt down those disks before you need to find them

in a panic.

In the end, I found a silver lining in this experience. The clean reinstallation of Windows cured my computer of some annoying glitches that it had developed and also improved performance markedly. But I wouldn't be so pleased if I hadn't been well-prepared for a failure.



provided by Connected (www.connected.com), offers both intelligent automatic backups and the additional security of off-site storage—safe from fire, theft, and computer failure—for about \$20 a month. As a bonus, I found their tech support extremely helpful when I ran into some minor problems in

BY PAUL CRAIG ROBERTS

MICROSOFT IS THE VICTIM OF A LEGAL MUGGING



TOP DOG:
Bill Gates's
success has
made him a
target for
antitrust
lawyers
schooled in
the belief
that business
is theft

Now that the Senate Judiciary Committee has set Bill Gates of Microsoft Corp. up as a robber baron, he and his company's shareholders can expect to be robbed.

There is no antitrust case against Microsoft. What is happening is that Sun Microsystems, Netscape Communications, and Novell are trying to achieve through antitrust politics what they could not achieve in the marketplace. Economists have known for decades that antitrust is what losers do to winners.

A genuine antitrust case requires a company to be a monopolist and to be convicted of acting in restraint of trade. For a company to restrain trade, it must face no substitutes for its product and be able to use its monopoly position to restrict output, raise prices, and block entry of new competitors. But in today's software industry, output is rising, prices are falling, and new companies are forming continually.

But facts have nothing to do with the government's antitrust cases. The Justice Dept. has an antitrust division that must find cases to justify its budget. According to *BUSINESS WEEK* (Jan. 19), the Justice Dept. "is relying on a novel theory" in its antitrust thinking about Microsoft. What that means is that Assistant Attorney General Joel Klein is, in effect, legislating the offense to fit Microsoft. He is creating the law as he moves along. Mr. Klein's approach is the opposite of a rule of law. A company cannot violate a law that is not on the books. If the Justice Dept. believes that new developments require new legislation, it should go to Congress and request new law, not write it itself and apply it retroactively to a preselected target.

Microsoft's success has made it a target for antitrust lawyers schooled in the belief that business is theft. Before Microsoft, there was IBM. The Justice Dept., in its unmitigated arrogance, tied IBM up for 19 years in an antitrust suit that the government never got around to defining. After forcing IBM to waste huge sums of money on legal fees and to run its business for two decades with an eye to legal considerations instead of the marketplace, the Justice Dept. ended up asking the court to dismiss its suit against IBM as "without merit."

The malfeasance in the Justice antitrust suit against IBM is so extraordinary that the department should have been abolished on

the demonstrated grounds that it is a clear and present danger to U.S. business.

This destructive scenario is set to repeat itself with Microsoft. Mr. Gates's time will not be reallocated from software development to lawyers and lobbyists, as Microsoft tries to fight off the political attack on its success. And every tort lawyer in the U.S. will figure out a way to piggyback a claim on the government's antitrust investigation.

The CEOs of Novell, Sun, and Netscape have shown poor judgment in encouraging the government to mug Microsoft. By bringing antitrust into software, these shortsighted executives have opened the gates of Silicon Valley to the redistributionist impulses of politics and regulation. The ingenuity and wealth of the U.S. software industry are the likely ultimate victims.

FAILURE TO CLONE. Microsoft is so far from being a monopoly that senators have coined a proxy term: "currently dominant firm." Microsoft is a currently dominant firm, but the reason lies in the mistakes of Apple/Macintosh, not in nefarious plotting by Microsoft. Apple Computer Inc. had the best operating system and a far more user-friendly computer. But the company's management made a business mistake. Apple refused to license companies to clone its product. This restricted output and made Macs relatively expensive. The result was a big market for the inferior PC, which Microsoft and other software companies exploited.

Capitalism in the U.S. has no future when CEOs of innovative companies appeal to the government to redress unequal market outcomes. To watch Sun's Scott G. McNealy behaving like a populist redistributionist whining for the government to give him an advantage or to take one away from a competitor is discouraging to those who fought to put supply-side incentives back into the economy.

The Justice Dept.'s investigation of Microsoft is an opportunity for ideologues who demand equal outcomes. The same quotas that are required for race and gender balance can be applied to product market share. Once merit is breached in one area, the case for it is weakened everywhere. Just as the market for air travel was once divvied up by "fair" government regulators, so can be the market for computer software. Whatever the outcome, Microsoft is sure to be in court long after it has lost its market dominance.

Paul Craig Roberts is a Senior M. Olin Fellow at the Institute for Political Economy and a Research Fellow at The Independent Institute in Oakland, California.



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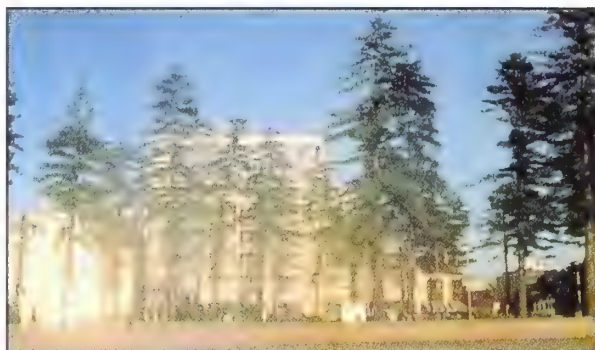
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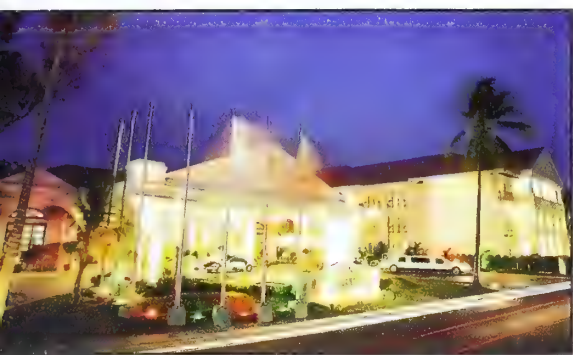
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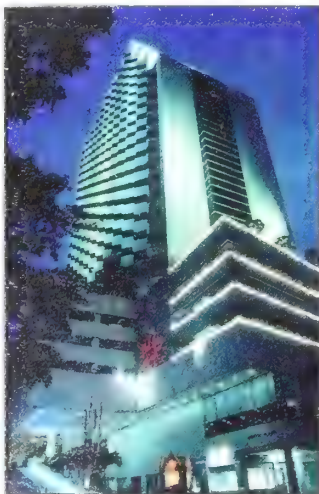

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NE KORETZ

DOWNSIZING'S PAINFUL EFFECTS

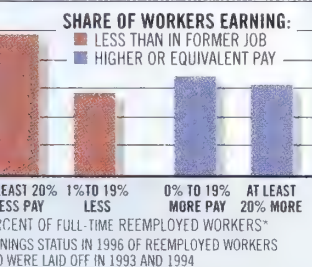
workers don't bounce back

With corporate layoff announcements up 38% over year-ago levels, it seems that downsizing is becoming a permanent aspect of U.S. labor life. So the fate of affected workers is more than passing interest.

The latest biennial Labor Dept. survey of displaced workers, which was conducted in early 1996, five full years after the current recovery began, illustrates the issue. Focusing on adults with permanent jobs (held at least three months) in 1993 and 1994, the survey found that about 3.2% of such workers had paid off in those years.

Otherwise, more industries and occupations were being hit with sizable job losses. Whereas manufacturing and blue-collar workers suffered the most in the 1980s, the share of layoffs affecting producing industries fell to less than 10% by the mid-'90s, with white-collar workers accounting for 60% of layoffs.

MOST DISPLACED WORKERS TAKE A HIT IN NEW JOBS



DATA: BUREAU OF LABOR STATISTICS

The good news is that by early 1996, many of workers displaced a few years earlier were back at work. An additional 14% were unemployed, and 14% had dropped out of the labor force. The least likely to be reemployed were displaced workers over 54, many of whom appear to have given up looking for work and opted for early retirement.

The bad news is that the trend toward downward mobility noted in earlier surveys hasn't abated. Of 2.2 million workers laid off in 1993 and only two-thirds had full-time jobs in early 1996. What's more, over half of this group were earning less than their former jobs, and over a

third suffered pay cuts of 20% or more (chart). Another sixth of former full-timers were either employed part-time or working at home, usually with sharply reduced earnings.

On average, median weekly earnings of full-time reemployed workers in the survey declined by about 14%—about the same as they did in a prior survey in 1994. Full-timers in their late 50s and early 60s who found new jobs, however, were particularly hard hit with pay declines averaging 37%.

To be sure, 47% of full-timers did as well or better in their new jobs, and 22% reaped pay gains of 20% or more. But the message of the latest survey results seems to be not only that downsizing in a modern dynamic economy is here to stay, but that it will continue to involve sizable and persistent earnings losses for many workers.

HOW HIGH ARE FAMILY TAXES?

A liberal-conservative debate rages

As a current spat between the conservative Tax Foundation and the liberal Center on Budget & Policy Priorities illustrates, taxes are a red-hot topic in the nation's capital these days. Piqued by recent statements by leading Republicans that taxes rose last year to more than 38% of the typical U.S. family's income, the center attacked the source of the figure—a Tax Foundation report on median income families.

In a 15-page analysis, the center criticizes the Tax Foundation's approach—particularly its stress on dual-earner families, which purportedly faced a total tax bite (all taxes at federal, state, and local levels) of 38.2% last year. Noting that the median income of such families came to \$54,910 last year, more than the incomes of two-thirds of all families, the center argues that it's more appropriate to focus on median-income families of all types.

According to the Congressional Budget Office, such families had an average income of \$36,942 last year and faced a federal tax rate of about 19.7%, compared with the 26.1% the Tax Foundation says two-earner families paid. So focusing on median-income families regardless of type would reduce the total tax burden faced by "typical" families by several percentage points, the center observes.

The center also quarrels with the treatment of corporate taxes. Rather

than allocating such taxes to families based on their ownership of stock and other corporate assets, as the CBO does, the Tax Foundation assumes that all families pay the same percentage of income as do wealthy families who have huge corporate holdings.

In its response, the Tax Foundation points out that it focuses on dual-earner families because that is the most common reporting type, and that it also includes single-earner families in its analysis. And it justifies its treatment of corporate taxes at federal and state levels by noting that some economists argue that corporate taxes are ultimately paid by workers through lower wages—so even workers who own no corporate stock are socked with corporate taxes.

As the debate goes on, the center seems to have scored a modest victory. In its rebuttal, the Tax Foundation reduced its estimate of the tax rate faced by dual-earner families last year by 0.6%, to 37.6%—the same as in 1995.

A PURRING GROWTH ENGINE

These seers see no downturn in '98

Although many forecasters see a significant slowdown in economic activity in coming months, the Economic Cycle Research Institute (ECRI) reports that its long-range gauge, designed to anticipate cyclical turns in the economy and project economic activity as much as a year ahead, skyrocketed in February to its highest reading since 1986. And its near-term gauge rebounded, as well.

The research group's indicators do point to some slowing in manufacturing and employment in the months ahead. But, says ECRI economist Anirvan Banerji, their overall strength suggests the economy will continue to post healthy growth through the end of 1998. He also dismisses fears of a severe stock market plunge, noting that ECRI's valuation yardstick indicates that stocks are not significantly overvalued relative to their behavior in past expansions.

TWO VIEWS OF THE TAX BITE

1997 TAX LEVELS



► PERCENT OF INCOME TAXED
*FEDERAL, STATE & LOCAL TAXES,
INCLUDES SALES, REAL ESTATE,
AND BUSINESS TAXES

DATA: TAX FOUNDATION, CENTER ON
BUDGET & POLICY PRIORITIES

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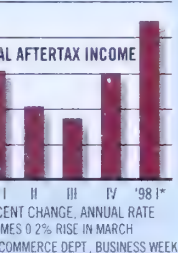
FOR CORPORATE AMERICA, REVERSAL OF FORTUNES

...y, earnings are under pressure, and U.S. households are in clover

U.S. ECONOMY

Up till now, the expansion of the 1990s had a familiar face: Corporate America downsized and invested its money to ever-higher profits, while Household America struggled to get ahead amid poor growth in real wages. That story is changing, perhaps dramatically. Businesses are having a much harder time earning a profit, even in an economy as strong as this one. Not only are earnings growing more slowly, but profit margins are also under pressure. At the same time, household income is surging, while tight labor markets and inflation push up real wages by the fastest pace in decades. That's quite a reversal: From 1991 to 1997, the real benefits of workers fell to the lowest share of total income since 1968, while the portion going to top profits rose to the highest level since 1968.

HOUSEHOLD INCOMES ARE SURGING



...y optimistic. Also, capital spending, a driving force in the expansion, has been fueled by robust earnings growth. Weaker profits, however, will cut capital budgets.

Meanwhile, consumers are having a field day, and there is little on the horizon to spoil the fun. While stocks suffer, real household income in the first quarter has risen at an annual rate of nearly 7% (chart). That would be the strongest quarter in five years, and the latest two-quarter gain is the largest in the decade. With help from an unusually warm winter, consumer spending looks to have soared at an annual rate of about 5.5% and February home sales jumped to a record level.

SHIFT BETWEEN PROFITS AND INCOME presents a tough problem for the Federal Reserve. The Fed is counting on the Asian crisis to cool off the economy, but consumers are powering a gusher of domestic demand that is offsetting the Asian impact.

Moreover, some companies may try to hike prices to help defray rising labor costs and shore up profits. The Fed left interest rates unchanged at its Mar. 31 meeting, but speculation is rising that the Fed may have readopted a formal bias toward future tightening.

The Fed is well aware of recent signs that the financial supports under the economy may be overly accommodative. Despite higher real interest rates and a strong dollar, liquidity appears to be flowing liberally through the economy: In particular, money growth is up sharply, and stock prices are up 13% this year. Also, competition among banks to make loans is brisk.

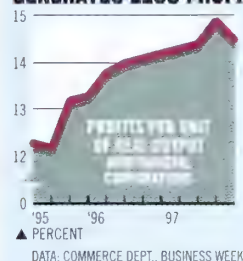
Moreover, the nation's purchasing managers report continued upbeat activity in the industrial sector in March. Their overall index rose to 54.8% from 53.3% in February, fueled by gains in production, new orders, employment, and slower delivery times. Although foreign bookings continued to weaken, overall orders strengthened amid surging U.S. demand.

BUT DESPITE THIS DOMESTIC VIGOR, profits are under pressure. Based on the Commerce Dept.'s fourth-quarter data on corporate profits, the squeeze may be severe. The data, reported on Mar. 26, seem like ancient history, given that companies are starting to announce their first-quarter profits. The Commerce report, however, which is based on the results of some 20,000 companies, showed some surprises.

First of all, fourth-quarter profits—adjusted for inventory values and the difference between tax-based and replacement-cost accounting—fell from their third-quarter level. That was the first decline since early 1995, when economic growth dropped below 1%, compared to this past fourth quarter's healthy 3.7% pace. Second, domestic operations accounted for two-thirds of the decline, while weaker foreign earnings were the remaining third. Finally, profits per unit of output took the largest quarterly tumble since 1995 (chart).

Unit profits are a kind of economywide profit margin that shows how much profit nonfinancial corporations generate from each unit of production. The percentage fell to 14.5% from a record 14.9% in the third quarter.

EACH UNIT OF OUTPUT GENERATES LESS PROFIT



ter. And with unit labor costs apparently having surged in the first quarter, further margin erosion seems likely. Indeed, profit worries are increasingly on the minds of investors in the stock market. The growing concern is that earnings will not come in strong enough to support the recent runup in stock prices.

THE EARNING POWER OF HOUSEHOLDS, meanwhile, reached new heights in the first quarter, and one of the warmest winters on record put consumers in the mood to spend. Real outlays for goods and services rose 0.3% in February, on top of a 0.6% advance in January. Even if March buying is flat, real outlays will rise at an annual rate greater than 5% for the second time in three quarters. In fact, the latest three-quarter run in spending will likely be the strongest in 13 years.

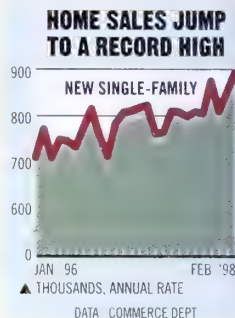
The question is: Can consumers keep up that heady pace? As long as jobs, incomes, confidence, interest rates, and the stock market provide a firm foundation, there is no reason why they cannot. Keep in mind, however, that the quarterly pattern of household spending has been up and down for the past five quarters, so second-quarter outlays will probably look softer.

That's especially likely because warm weather in the first quarter pulled forward some buying that normally would have occurred in this quarter. March retail surveys show cooler sales than in January and February, as more normal weather returned to much of the

country. In addition, March consumer confidence did decline, but the February level was a 29-year high.

The weather has magnified the gains in the already vibrant housing market. Sales of new single-family homes jumped to a record annual rate of 893,000 in February (chart), and purchases of existing homes hit an annual rate of 4.75 million, also a record. Those levels are unlikely to hold up in the second quarter. But that will not mean that housing is weakening, only that El Niño is loosening its grip. Housing starts should remain strong since the inventory of unsold new homes was at record low in February.

The great unknown in the changing fortunes of consumers and businesses is productivity. Greater productivity growth would allow healthy profits and more household buying power to occur at the same time. But given that earnings are already showing signs of strain, the upcoming data on productivity could be disappointing. And if profits slipped during the robust fourth quarter, Corporate America will face tougher challenges in 1998 as the economy slows, even as Household America enjoys its new prosperity.



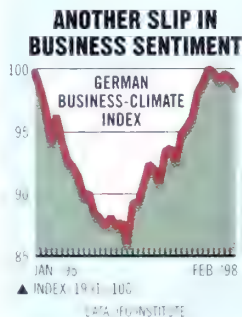
GERMANY

PLODDING ALONG TOWARD RECOVERY

The tortoise-like recuperation in Germany continues to crawl along, with the latest signs suggesting that Asia is crimping growth but not crippling it.

Exports fueled Germany's real gross domestic product to a 2.3% gain for all of 1997. But the Asian crisis is causing some fear among businesses: The IFO Institute's business confidence index fell again in February, the fourth drop in the past five months (chart). Asia's effect, however, is less clear in other data. Machine orders, for example, rose 14% in February from a year ago, with export demand surging 24%. Domestic orders were up only 2%, raising fears that the capital-spending

boom may be losing steam. Even so, first-quarter real GDP likely grew at a quarterly rate of about 0.8%. The strength reflects a rebound after the fourth quarter's anemic 0.3% gain and unseasonably warm weather that lifted retailing and construction.



In coming quarters, the labor markets, not weather, will guide domestic demand. Unemployment is dropping a bit this year after the pan-German jobless rate hit a

record 11.8% in the fourth quarter. Job vacancies are up, which could be supporting the rise in consumer confidence. And unions are beginning to approve concessions in order to avoid job cuts. Germany's 3.2 million public

workers accepted pay raises about equal to the inflation rate in return for some job stability.

Overall, inflation remains tame. Consumer prices rose just 1.1% in the year ended February, thanks in part to falling oil costs. Core prices, which exclude food, fuel, and administered costs, show a small uptrend, but not enough to worry the Bundesbank. Instead, the Buba is focusing on the European Monetary Union and the stability of the euro. In order for European interest rates to converge by May, the Buba is expected to keep its rates unchanged.

The Buba is worried about the mark's fall vs. the British pound, although the slide may help exports to the rest of Europe. At the same time, domestic demand looks healthy enough to keep the slow-but-steady upturn going.

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THE JOLT JAPAN NEEDS?

Its slump is now so bad that Tokyo may be forced to make real changes

The crisis of Japanese capitalism is lurching into a new and dangerous stage. Every sign points to a deep recession, the worst contraction the country has seen since the oil shock of 1974. Investors are losing faith in the government: Between March 26, when Prime Minister Ryutaro Hashimoto announced a \$120 billion stimulus package, and April 1, the Nikkei tumbled 4.3%, and the yen weakened 4%, to 133.6 against the dollar. The markets figure Hashimoto will not deliver a needed tax cut, but opt instead for public works that give little lift to the economy. And businesses are bracing for one of the worst months ever, as companies close the books on their fiscal year and report record losses and writeoffs.

Pressure is building from other quarters. Japan's Big Bang financial market liberalization, which kicked off on April 1, may give ordinary Japanese a chance to dump local stocks and bonds and invest overseas. That would further weaken the yen and the markets. U.S. policymakers may react strongly if the falling yen pulls Asia's other battered currencies into another dizzying fall. Taken together, the factors are there to force Japan's leaders to cut taxes and deregulate the economy further.

A huge shock may be necessary to

jolt the Japanese out of their policy paralysis. For now Tokyo is following the same old script. The ruling Liberal Democratic Party promises real action; the markets react with disbelief; the economic data get more and more alarming. The U.S. provides the background chorus, warning Japan to change, to cut taxes, to deregulate, to do something. Commentators then note the LDP is too beholden to special interests in the construction industry and its rural constituents to back anything other than more pork for public works.

The old formula used to work well enough, despite the criticism it provoked. The Ministry of Finance was able to divert enough public money into the markets to boost confidence, and use its enormous influence to keep local investors from running. But now the MOF itself is under siege by prosecutors probing for evidence of corruption. There's little belief in any quarter that the MOF and its LDP allies can defuse the latest economic crisis. The government wanted the Nikkei at 18,000 before the end of the fiscal year on Tuesday, Mar. 31. Instead, it closed at 16,527.

The markets are paying a lot more attention to the worsening business news than the government's posturing. Take the banks. The government has softened accounting rules so it's easier for them to meet capital requirements. But investors still view the banks' balance sheets as sus-

pect, and the banks remain wary of making fresh loans. So Japan's terrible credit crunch will continue. In a March survey of 1000 companies by the Ministry of Finance, 40% said they were facing far tougher lending terms, and 38% said the scarcity of credit was hurt-



Shaky Prospects

ing their businesses. The latest casualty is Daiichi Corp., a real estate lender and broker. Burdened with sour property loans of some \$3.3 billion, it filed on April 1 for liquidation after its main creditor, Mitsui Trust & Banking Co. Ltd., cut it off.

WEAK DEMAND. The news is going to get worse. Industrial production contracted 3% in February. Consumers are not spending. The jobless rate is at record 3.6%. The betting is that it will reach 5.2% next year. Corporate profits for the fiscal year that ended Mar. 31 are expected to plunge 15%. Mitsubishi Electric Corp. will probably announce 1997 loss of \$680 million, because of weak demand for its appliances and troubles at its chip unit. Toshiba will likely report its pretax profits fell 64%, to \$77 million.

Reading the signs, J.P. Morgan & Co. and HSBC-James Capel are now telling their clients to run for cover. J.P. Morgan economist Jesper Koll sees



**GOING TO WORK:
COMPANIES REPORT
RECORD LOSSES
AND WRITEOFFS**

GROWTH

GDP contracted 0.5% year ending in March. No growth expected for 1998.

Nikkei index crashing 25%, to 12,000. Bear market. Says Andrew Shipley, an economist with Schroders Japan Ltd., "The markets are just falling apart."

There is also a real risk that Japan will face a currency crisis of its own. The yen is at its weakest level in more than two years. Analysts are looking at a drop to 150 by June, as the economy weakens more and policy drift continues. An important change may be one change in the partial deregulation of the financial-services industry that started in April 1. Under newly liberated foreign-exchange rules, ordinary Japanese will have a far easier time swapping yen for foreign currency and sending money abroad. That could send a wall of yen out of Japan in search of richer investments. Pensioners and boomers, dissatisfied at the puny returns on their domestic bonds and savings deposits, may be more inclined to invest in U.S. securities. The prospect of a dramatically weak-

CORPORATE FAILURES

Bankruptcies spiked up 32% in February; have been increasing for 14 months.

er yen is even frightening some of Japan's politicians. "Japan's economic situation, as well as Asia's, is now in danger," says Naoto Kan, Japan's most powerful opposition politician. He says the LDP could trigger a new Asian crisis if the weak yen forces other regional governments to devalue to keep exports up. American policymakers cannot afford a weak yen either. Weaker currencies in Asia mean more cheap exports to the U.S., much weaker demand for American-made goods, and the threat of a new regional banking crisis.

TAX-CUT CHORUS. This all means pressure—more pressure than the LDP and the Ministry of Finance have probably felt in decades. Naoto Kan echoes the opinion of most economists by calling for a massive tax cut of at least \$45 billion annually for several years and an end to the corrupt connection between the LDP and its backers in the construction industry. So far, LDP elders

POOR EARNINGS

Profits for fiscal year are down 15%, and there's more bad news ahead as Asia weakens.

RIISING UNEMPLOYMENT

Jobless rate now at a record 3.6% and could hit 5.2% by next year as companies restructure.

are balking at any big policy shift. But a contraction that threatens to turn into a collapse could change their minds.

Skeptics point out that the Japanese system can endure repeated blows without changing. The government-managed postal savings system has \$3.2 trillion in deposits. That gives Tokyo leverage to ride out the storm by borrowing from postal savings to bail out banks, build more bridges, and generally avoid a wholesale rearrangement of the economy. Tokyo has pumped more than \$550 billion into various packages since 1993. That's roughly twice what Germany spent on reunification.

Yet only recently have the Japanese faced record rates of bankruptcy, a cracking banking system, a collapse in consumer spending, and a regional crisis. It's getting ominous. This time, even Japan's mandarins may not be able to keep the world at bay.

By Brian Bremner in Tokyo

THE ECONOMY

THE FED MAY HAVE SOMETHING TO WORRY ABOUT

Is the money supply's spike troubling? Some economists say so

Despite the Federal Reserve's secretive reputation, there was little suspense surrounding its Mar. 31 session: For the eighth consecutive meeting, policymakers opted to...do nothing. With the economy still in a blissful state of strong growth and low inflation, some Fed watchers believe the policymaking Federal Open Market Committee could stand pat for the rest of 1998.

Yet there is at least one troubling cloud on the horizon: a sharp and so far unexplained jump in the nation's money supply (chart). A few economists believe that the marked trend might be a sign that the breathtaking runup in stocks and other asset prices is spilling into the broader economy. If so, that could trigger a rise in inflation.

On Mar. 16, Allan H. Meltzer and other prominent monetarist economists—who see money flows as a leading indicator of economic output—called on Fed Chairman Alan Greenspan to raise interest rates before the economy starts to overheat. “The seeds of high inflation have been and are being sown,” said the group, known as the Shadow Open Market Committee. “It is irresponsible to ignore the increased money growth of the past six months.”

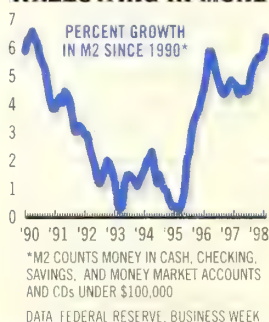
If Meltzer and his fellow monetarists are proven right, it would serve as sweet vindication for a once-proud theory that has flirted with irrelevancy over the past decade. During the early 1980s, Fed Chairman Paul A. Volcker cited the soaring money supply when he raised interest rates to double digits. But Volcker was never a true monetarist, and Greenspan has largely ignored money measures since the early '90s. He has argued that the shift by consumers into mutual funds, which are not counted in the money supply, broke the supply's link to gross domestic product.

But monetar-

ists argue that growth in M2—the best measure of currency, checking accounts, and most savings accounts—has over the past year come back into sync with the pace of GDP. If true, the spike in money-supply growth could fuel a surge in output and inflation. Since December, M2 has been climbing at an 8.3% annual rate—its fastest rise since 1989 and above the 5% ceiling many monetarists deem prudent.

Even some economists who don't consider money growth troubling still worry that it could turn the slightest inflationary spark into a bonfire. “It provides the fuel for a bigger inflation problem,” says First Union Corp. economist David Orr. “The more liquidity there is, the harder

WALLOWING IN MONEY



it'll be for the Fed to mop it all up.

Still, most economists aren't alarmed by M2's surge—yet. They attribute the recent spurt to temporary factors, including the flight of Asian investors from the dollar and the recent boom in mortgage refinancings. Taxpayers with large capital gains and corporate bonuses are likely building up their checking accounts to write big checks to Uncle Sam as well. **“TOO EASY.”** What's more, some forecasters contend that current money growth is more a sign of healthy demand than of inflation. Rising money

would be worrisome, says Brian S. Wesbury, chief economist for Chicago-based Griffin, Kubie, Stephens & Thompson Inc., if gold and other commodity prices were soaring, the dollar was plummeting, and inflation-adjusted interest rates were relatively low—in 1994. Then, the Fed did embark on an aggressive round of rate hikes to head off inflation.

But now, gold is falling, real interest rates are high, and the dollar is soaring. “Of all the key monetary indicators, money growth is the only one that suggests Fed policy is too easy,” says Wesbury.

Fed policymakers concede that they're intrigued by the closer correlation between M2 and GDP. Greenspan admitted in February that there were “tentative signs” of a closer link between money and output—but questioned “the stability of the relationship.”

As a result, the Fed isn't ready to re-adopt the money supply as a guide for policy. The Fed's resident monetarists, regional Fed bank presidents William Poole and Jerry L. Jordan, are handily outvoted by Greenspan and other economic pragmatists. And Federal Reserve Bank of Dallas President Robert D. McTeer Jr. told a Florida audience on Mar. 27 that “with all the financial innovations we've had, it's very hard to know what the right rate of growth of the money supply is.” Until the Fed's money mandarins figure that one out, M2 may remain something of a relic.

By Dean Fort
in Washington



By John Carey

GIVE GREEN TAXES A GREEN LIGHT

Suggesting a carbon or gas tax has long been political poison. But that doesn't seem to be deterring legislators in Vermont, Minnesota, and Maine. All are debating or pushing bills that would levies such as property or income taxes and make up the revenue with taxes on fossil fuel.

The chances of passage for any of the legislation anytime soon are

slim. That's unfortunate. Such conversions to "green" taxes could be just what the country needs. Energy use imposes hidden costs—such as the health costs of pollution, lost productivity from traffic congestion, and the threat of global warming—which aren't reflected in its price. "Taxes on resources correct one of the most glaring flaws of market economies: blindness to environmental costs," argue Alan Weintraub, Durning and Ram Bauman in a new book *Tax Shift*. The beauty of tax-shifting is that the overall tax burden stays the same: the new "green" taxes are balanced

by cuts in other taxes. Economists generally agree that payroll, income, property, and other taxes discourage investment in labor and capital. Cutting these taxes could thus spur productivity and growth while the new taxes bring environmental benefits. "There may not be a free lunch, but there is almost certainly a lunch worth paying for," says Stanford economist Lawrence H. White.

Some green taxes are on the books overseas. Since 1996, the Netherlands has been raising about \$1 billion annually with a gas and electricity tax—and returning it with cuts in Social Security premiums. That's proven too small to lower consumption appreciably, says Dutch en-

vironmental official Pieter Maessen, so the country plans a \$1.7 billion boost to the tax. Similar tax shifts are on the books in Denmark, Finland, and Sweden.

The U.S. has been less adventurous. But states are exploring options. In Minnesota, a proposed revenue-neutral bill would slash property taxes by about 25% in exchange for a \$50-per-ton tax on the



CLEANER AIR Imposing energy taxes while cutting other levies would help the environment and the economy. Many studies of such taxes show a net benefit

carbon in fossil fuels. That translates to a tax of 4¢ to 5¢ per gallon on gasoline, or a 25% increase in the price of coal. In Vermont, legislator Ben Rose has introduced a bill which would impose a \$100-per-ton carbon tax with cuts in other levies. Legislators in Maine are contemplating similar measures.

BURDEN. Unfortunately, business dislikes these ideas. When Minnesota legislator Ann H. Rest proposed replacing payroll taxes with an energy tax in 1996, coal interests tarred the plan as a burdensome tax increase. Since then, Rest and her backers have armed themselves with economic studies showing a net benefit to the state and made the measure more politically attractive

by targeting the property tax for cutting.

There are problems with tax-shifting: Some energy-intensive manufacturing industries would be harder hit than high-tech companies. "This is an antibusiness proposal," fumes Northwest Airlines Inc. spokesperson Kathy Peach, who pegs the cost to the company at \$47 million per year. Even companies such as Honeywell

Inc., which stand to benefit from the legislation by selling more energy-efficient equipment, are against the bill. "We can't solve these problems on a state-by-state basis," explains Glen Skovholt, vice-president for government and community affairs for Honeywell.

Another worry is that lawmakers won't deliver on tax cuts once the "green" taxes are in place. The Dutch energy tax hike "is like the nose of the camel [under the tent]," frets economist Wiel Klerken of the Dutch Employer's Assn., while the tax cut "can be reversed at any time." But it's easy to guarantee that all tax

shifts be revenue-neutral.

Taxes have always favored one sector or group over another. So why not use the carrot and stick more wisely? If energy consumption taxes replaced income and sales taxes, people could reduce their tax burdens by becoming more energy efficient. "People could earn more and spend more and yet pay less tax," explains M. Jeff Hamond, director of fiscal policy at liberal think tank Redefining Progress, which is holding a tax-shifting symposium in Washington on Apr. 7. It's about time Americans were given that choice.

Carey covers environmental issues in Washington.

INTERVIEW

ANDY GROVE TALKS ABOUT HIS NEW LEARNING CURVE

The Intel founder goes from the daily grind to the big picture

Andrew S. Grove has made his mark as a manager, but now he's turning himself back into a student. The chairman and chief executive of Intel Corp. announced Mar. 26 that he will hand over the CEO job to Intel President Craig R. Barrett in May. The change, Grove hopes, will let him spend more time studying the computer industry—and helping to guide the evolution of technology and public policy. For Intel, freeing Grove to drink up technology trends could help it avoid missteps like its slow response to the rise of sub-\$1000 PCs. On Mar. 31, *BUSINESS WEEK* correspondent Andy Reinhardt talked to Grove about how the executive plans to spend his future.

Q: Why step down as CEO now?

A: I've been CEO for 11 years, and there is a repetition and sameness to the rhythm of the job. Just think how many operations reviews, financial reviews, routine meetings, demand forecasts, etc. I have sat through. I was ready to change my routine. I'll have more leeway in my schedule.

Q: What will you do with your extra time?

A: It's a rearranging of priorities: I can meet somebody that otherwise I might not have had time to, or I can go look at somebody's work that otherwise I wouldn't have. I don't know exactly what I'm going to do—I just know that I'm craving that kind of flexibility.

Q: What topics are you especially interested in these days?

A: The future of networked computing, especially in businesses that haven't used it, and what we can do to remove obstacles to using it. Understanding the potential of various technologies, and the deployment of those technologies en masse. I can talk casually about any of those subjects,

but my understanding is not that deep. I'm painting a canvas with my eyes closed.

Q: What else do you plan to explore?

A: Commerce, marketing, information, entertainment—all of these things are going to be impacted by the presence of a billion connected computers. What needs to be done to reach that point sooner rather than later? Bandwidth has to be generated and dispersed to individuals and small companies. I want



to understand this better. I also want to have a better appreciation for what type of applications will be deployed as this connected PC world gets rolled out. The only way I can ever find out about those is by hanging around with people inside and outside the company who are into application development.

Q: Can you think of an example when Intel would have benefited from better trend-spotting?

A: We were an early player in cable modems, which had the potential to deliver bandwidth to consumers. We were one of the first ones to demonstrate working cable modems five years ago,

but I don't think we understood the task in its entirety. I would like to understand what it takes to do these things a little better.

Q: Are you also putting more emphasis on cultivating software developers?

A: Absolutely. We've done a very good job with game developers, historically. We put technology, muscle, sometimes money, into funding advanced games. I'd now like to see that type of activity replicated in different fields, especially in applications pertinent to small- and medium-size businesses.

Q: Will you get more involved in policy?

A: Yes. These changes [from connected PCs], as they permeate society in the U.S. and abroad, will be so significant that they're going to be an increasing focus of regulations and government actions. I think we as an industry

“Commerce, marketing, information, entertainment—all of these things are going to be impacted by the presence of a billion connected computers.”

have a responsibility to guide that.

Q: Your first-quarter earnings warning suggests changes ahead. Will Intel still get most of its revenues from microprocessors in five years?

A: Yes. There's an enormous temptation to take the events of a quarter and extrapolate them. But it's wrong when a couple of bumps in the road lead you to question the essentials. I think the development of low-end computers is going to be an important element of the market, but it's just one element. There will also be performance PCs and mobile PCs, and servers will be the underpinnings of all of them.

MOTOROLA GIRDS FOR A SHAKEUP

Executives mull an overhaul to get it back on track

Year ago, with his company slipping from its perch atop the wireless industry, Motorola CEO Christopher B. Galvin tried to mobilize the company. He issued a memo demanding worldwide sales and earnings growth of 20% a year. The goal, however, was still a long way off. Motorola's sales improved a lackluster 6.5% the year before, and the company repeatedly failed to meet Wall Street's expectations. "That sends a strong signal to investors that Motorola doesn't have everything under control," says one Chicago-based institutional investor.

To get the company back on track, Galvin wants to make a sweeping restructuring. The overhaul would combine disparate operations within the company's wireless business—segments that make up more than 60% of Motorola Inc.'s overall sales. Historically, mobile phones, paging, and two-way radio operations have existed as separate—and warring—factions. Each unit has its own network equipment team and a group for developing the actual handset or pager operated by the end user. But within the next several weeks, Motorola is expected to shift all network equipment operations into one division, with the development and manufacture of the handsets, pagers, and radios folded into another unit.

THE DOOR. Galvin's plans are complicated by the surprising departure of a key executive. On Apr. 1, Jack M. Scanlon, president of Motorola's mobile networks and space business, announced that he was leaving the company to run telecommunications startup Global Crossing. Analysts and insiders figure that Scanlon would have headed one of the two divisions that are expected to be created in the overhaul. Motorola is likely to appoint Merle W. Moore, head of European operations, and James A. Norling, who runs Motorola's messaging segment, to lead

the soon-to-be created units, insiders say.

The reorganization would address Motorola's chief problem: sluggish execution in an increasingly competitive wireless market. In March, unreliable network equipment contributed to the loss of a \$500 million contract with digital cellular carrier PrimeCo Personal Communications. And the company has yet to deliver its popular StarTac phones with CDMA digital technology—a high-capacity system that is gaining popularity in the U.S.

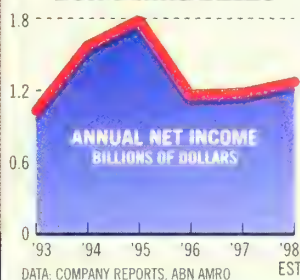
Since taking the reins as CEO in late 1996, Galvin has labored to fix Motorola's deficiencies. Not having digital handsets caused the company's U.S. market share in cellular phones to slip from 51% in 1996 to 34% in 1997, according to wireless consultants Herschel Schostek Associates.

The company has also lagged behind competitors in some key technologies. Motorola doesn't make its own digital switch, using instead ones that are produced by Digital Switch Corp., which,



CEO GALVIN

MOTOROLA'S NUMBERS DON'T RING BELLS



industry executives say, lack the sophistication of the equipment made by rivals Lucent Technologies Inc. and Northern Telecom Ltd. By combining the wireless network equipment segments into one unit, Motorola could potentially justify developing its own switching equipment.



Such improvements would help Motorola capture more of the world's \$30 billion network equipment market, where its share has dropped from 21% in 1996 to about 17% last year, according to UBS Securities Inc.

The proposed overhaul is being applauded. "I think they've recognized what customers are telling them," says Gary Cuccio, chief operating officer of Omnipoint Communications Inc. "This seems to be a first step in a genuine effort to improve their position."

Analysts agree that streamlining wireless segments could breed better internal relations and might achieve some cost savings.

But it's not a panacea. "At the end of the day, Motorola needs to execute more intensely," says ABN Amro analyst Kenneth Leon. "They need to get the products out quicker." With the whole world watching, Galvin can't afford any more false starts.

By Roger O. Crockett in Chicago

By combining divisions, the company hopes to get products out faster in the competitive wireless market

LEGISLATION

AN OFFER BIG TOBACCO CAN'T REFUSE?

A tough new compromise may be the best the industry can get

Judging by the howls coming from Tobacco Road, compromise legislation unveiled by Senate Commerce Committee Chairman John McCain (R-Ariz.) on Mar. 30 will bankrupt the tobacco industry and spawn a black market in smuggled cigarettes. McCain's plan toughens last year's settlement between tobacco lawyers and states by requiring a \$506 billion payment by cigarette makers while denying them much of the legal shield from class actions that they want. "The extreme positions in the McCain outline are very disappointing," says industry negotiator J. Phil Carlton.

So will Big Tobacco's opposition snuff

Lawmakers from both parties have an enormous stake in completing a deal now that they've made plans to spend the settlement windfall

ate floor. "This is our last, best effort to get the tobacco settlement done," says Mississippi Attorney General Mike Moore, who helped craft the June, 1997, proposed settlement between tobacco lawyers and 40 state attorneys general.

McCain's compromise would cap at \$6.5 billion the amount the industry could be forced to pay annually in legal damages—\$1.5 billion higher than the '97 deal. It would permit class actions and punitive damages barred by the June accord. And it would give the Food & Drug Administration power to regulate tobacco products. Wall Street reacted quickly: Tobacco stocks plunged, and bond ratings were downgraded.

Tobacco executives and Wall Street analysts are now scrambling to decide whether the industry is better off accepting McCain's plan or abandoning the deal in order to fight legal battles on a state-by-state basis, with all the uncertainty that brings. Sanford C. Bernstein & Co. analyst Gary Black says industry

shows. It's an all-or-nothing strategy that could prove counterproductive: executives walk away and lawmakers make the bill even tougher.

Already, many Republicans are dashing for cover as Democrats bash them for taking millions in tobacco contributions. Indeed, McCain's proposal is clear evidence that the industry's \$30 million in donations since 1987 can no longer buy happiness on Capitol Hill. "I can and will never be subject to a veto by the tobacco industry," says McCain. And if McCain's tough stance wasn't convincing, certainly the Senate's overwhelming approval on Mar. 31 of a resolution declaring that cigarette companies should not be immune from lawsuits ought to be a wake-up call.

Some of Big Tobacco's wounds are self-inflicted. For one thing, the industry misjudged the political climate. "I underestimated the pure hatred for the industry that is out there," says Carlton. On Capitol Hill, Republican leaders and pro-tobacco Democrats remain furious that the industry excluded them from last year's settlement talks. And House Speaker Newt Gingrich has told his leadership team that he won't allow Democrats to outflank him on the issue.

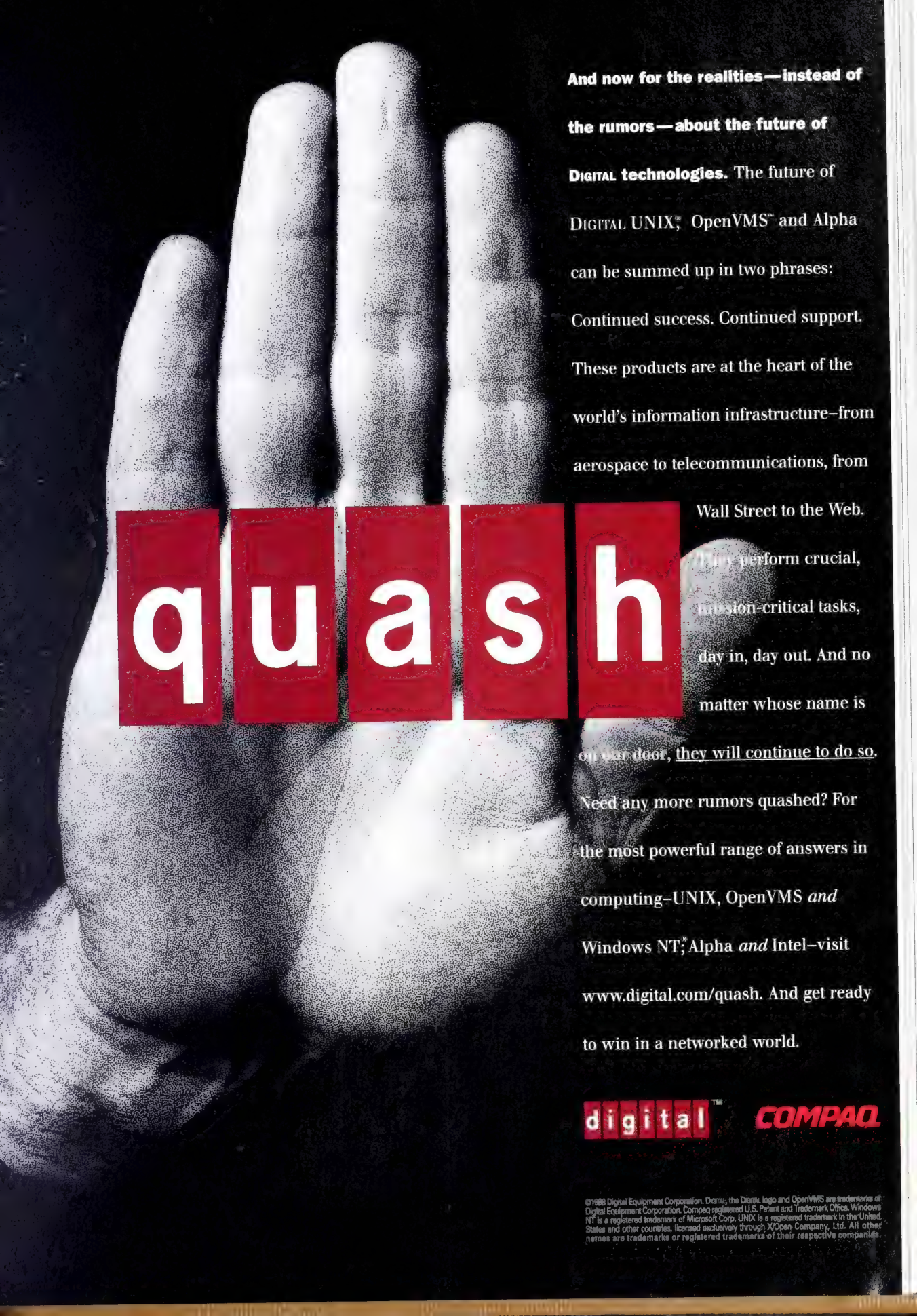
Tobacco negotiators are realizing some legislation is likely with or without their support. That's quite a comedown for what was once the toughest industry lobby in town. Now, Big Tobacco has a choice: Keep fuming or start dealing.

By Richard S. Dunham in Washington, with David Greising in Atlanta and Gail DeGeorge in Miami

out legislation? Not likely. The industry may be forced to accept the McCain proposal as the best vehicle—still being offered—to rid itself of a growing backlog of civil suits. Tobacco's erstwhile GOP allies, worried that their industry ties will hurt them in this fall's elections, are in no mood to be generous. And lawmakers from both parties are eager for a deal now that they've made plans to spend the settlement windfall. "This is the best deal tobacco's ever going to see," concedes a tobacco-industry source. "BEST EFFORT." McCain's consensus bill is a watershed in the yearlong debate over a possible settlement of legal claims against tobacco companies. And on Apr. 1 it was overwhelmingly approved by the Commerce Committee with the bipartisan support it needed to reach the Sen-

earnings would fall 20% the first year after the McCain legislation would take effect, and 36% by the fifth year. Still, analysts say Big Tobacco desperately wants a cap on liabilities to bolster share prices. Even industry-friendly Hill staffers are urging the companies to sign on. "Tobacco has missed out on the stock market boom of the '90s," one staffer says. "It's time for them to get on board."

But many in the industry are not ready to buy those arguments. The companies plan to attack McCain with a media blitz, a lobbying offensive, and tobacco CEO appearances before editorial boards and on morning television



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BROADCASTING

IF THESE SHOWS ARE HITS, WHY DO THEY HURT SO MUCH?

As network viewers defect, advertisers may not foot the big bills

To understand the state of play in TV Land, look no further than the kids' market. Normally, the annual negotiations to set ad rates for children's network TV shows wrap up in February, with over 90% of all the ads sold. But at the end of March, as a crush of new channels from WB to the new Fox Kids Network were depressing ratings, many advertisers were still waiting for ad prices to sink lower. "The market is soft. Why should we rush into it?" says Bill Croasdale, president of Western Media International, which buys ads for clients that include Home Depot, Acura, and Walt Disney.

Not surprisingly, it is with some apprehension that the TV industry is heading into this year's so-called prime time "upfront market," where networks trot out their shows for September and advertisers line up to buy as much as half of the networks' \$14 billion in advertising time in advance. This year, the line isn't expected to form so quickly. Network ratings are down once more. And just as in the kids' market, primetime is packed, with cable channels such as USA and TNT and upstart networks like WB. Today, just over half the country's 97 million homes tune into NBC, ABC, CBS, and Fox, down from 75% only eight years ago. "From where I am sitting, it looks like a buyers' market," says Croasdale.

GRIM SPRING. Meanwhile, the networks' programming costs are spiraling after a winter of heavy bidding to win the rights to air such programs as National Football League games, *ER*, and *Mad About You*. The likely result: plummeting earnings. Merrill Lynch & Co. analyst Jessica Reif Cohen expects operating earnings for the Big Four to plummet 68% in 1998. Only CBS will show an improvement, and the network will still post a loss.

Prices for the upfront market won't be determined until late May. But already, the maneuvering is starting. NBC, trying to offset the \$13 million it's paying for each *ER* episode, is said to be asking \$650,000 for a 30-second spot. CBS and Fox are asking for 20% higher ad spots on their football tele-

casts to help pay for their \$18 billion three-year deal with the NFL. However, odds are the networks won't get that much. Instead, networks will likely use the ultra-expensive shows, such as ABC's *Home Improvement*, as loss-leaders to prop up or promote other shows.

The Big Four began courting advertisers in late March with flashy cocktail parties and video clips of pilots in development. NBC is mulling which show to use to rebuild its *Seinfeld*-less Thursday night lineup, while ABC is overhauling huge pieces of its still-struggling prime-time programming. CBS is developing sitcoms with an eye to younger viewers starring such actors as Melanie Griffith and Arsenio Hall, while Fox hopes to reverse a 10% drop in its ratings with a futuristic animated show from Matt Groening, creator of *The Simpsons*.

DUELING DOGS. But even if all the shows work, the competition is gaining. Cable, which last year sold \$2.4 billion worth of ads in the upfront market, has near-network ratings with shows such as Comedy Central's *South Park*, which command \$70,000 for a 30-second spot. And by September, the TNT cable network will be showing reruns of *ER* five nights a week, including a planned Thursday night airing opposite the NBC original.

The Big Four will have other competition this fall. Univision, a Spanish-language network, took \$200 million last year in upfront ad buys and will likely do better this year. Meanwhile, ratings at WB have exploded, gaining 27% on the strength of a Tuesday night lineup that includes teen hits *Buffy the Vampire Slayer* and *Dawson's Creek*. The latest *Beverly Hills 90210* wannabe, *Dawson's Creek*, has been able to sell 30-second spots for an impressive \$200,000.

Despite their ratings slide, network executives still think they can negotiate rate hikes. "Our strength will always be that we can deliver more eyeballs," says Joseph D. Abruzzese, president of network sales for CBS. NBC Chairman Robert C. Wright made the same point to reporters in January, just after he plunked down \$850 million for three years of *ER*. That was right after he opened his remarks by getting down on his hands and knees in a mock prayer to ask the TV gods to deliver Helen Hunt and Paul Reiser for another year of *Mad About You*. They did, and it cost Wright \$2 million a week for the two stars. His next prayer should be for the networks' ratings to perk up.

By Ronald Grover in Los Angeles

WORKING AGAINST THE NETWORKS



Salaries for stars like *Mad About You*'s Helen Hunt and Paul Reiser will hurt profits at NBC

PRICE OF A SPOT: \$275,000



Dawson's Creek, a new WB show, is luring kids away from the big networks

PRICE OF A SPOT: \$200,000



Comedy Central's hit, *South Park*, beat ABC's *PrimeTime Live* in February

PRICE OF A SPOT: \$70,000



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WINNING THE HEARTS OF THE WORLD



MEDIA

McPAPER NORTH?

A Canadian daily wants to be an upscale *USA Today*

Following an old journalistic maxim, press mogul Conrad M. Black likes to afflict the comfortable—at least when the comfortable run rival newspapers. His *Chicago Sun-Times*, *Jerusalem Post*, and London *Telegraph* group have made some inroads against more upscale or widely read competitors. Now, the Canadian is about to shake up the news business at home. In early April, he is expected to take a page from Gannett's 16-year-old *USA Today* and announce plans for a Canadian national daily.

Canada Today—as some rivals disparagingly call his so-far unnamed paper—is already making waves. The country's leading national daily, the *Globe and Mail*, and the big-selling *Toronto Star* have been upgrading their pubs for months. Since the main battleground will be Toronto, home of four papers, a newspaper war seems unavoidable. Says John A. Honderich, pub-



BLACK: "To sell 300,000 more [papers] doesn't seem...too high a mountain"

lisher of the locally focused *Star*: "The pressure is going to be huge for some kind of rationalization."

In fact, Black's own empire—the third-largest newspaper operation in the world behind News Corp. and Gannett—will feel some heat. Through his \$2.2-billion-a-year Chicago-based Hollinger International Inc. and its 58.6%-owned Canadian subsidiary, Southam Inc., Black controls 55 U.S. and 63 Canadian dailies. And the new paper will almost certainly take ad dollars and readers from some of his other

Canadian operations. "There is potential cannibalization on advertising, but we think it's manageable," says Donald Babick, publisher of the *Vancouver Sun* and *Province* and president of Southam.

Still, Black, 53, has critical advantages. With Hollinger operating income up fourfold since 1995, to \$287.2 million, he can easily absorb the \$70 million or so in costs from the new venture over the next five to eight years. He'll use his local presses to print the daily while distributing it with the local papers. And he'll aim it at more upscale readers. "We sell 2.4 million papers a day in the country now," he says. "To sell 300,000 more doesn't seem, on its face, too high a mountain to climb."

Black admits launching the newspaper would be a "slog." Gannett's *USA Today* cost "hundreds of millions of dollars" and took five years to show a profit, says founder Allen H. Neuharth. Black expects losses to be lower with profits likely in just a few years.

Unlike Neuharth, Black won't have much flag-waving nationalism to bank on among the less fervent Canadians. The mogul says many of his countrymen feel a "comparative lack of national cohesion." But he adds: "We can help to fill that gap." If he does, his discomfited rivals may see a few gaps of their own.

By Joseph Weber in Toronto

DETROIT

LINCOLN'S \$50K PICKUP

Ford has a better idea (maybe): A luxury truck

Lincoln, the luxury car line once believed to be sailing into the sunset, is finding new life by redefining the land yacht. Its sales have soared 48% in the 1998 model year thanks to its new Navigator sport-utility vehicle. Now Ford Motor Co. believes it has an even better idea: a Lincoln luxury pickup truck.

Ford is developing a \$45,000-to-\$50,000 pickup it calls the Lincoln Blackwood, say sources close to the company. Aimed at the horsey set, it combines the Navigator's chrome-grille with a short, black-varnished wood truck bed. The four-door passenger area looks like the Ford pickup, but with a leather-and-walnut interior.

A company official con-

type was developed, but declined to say if it will actually be sold. But sources familiar with Ford's plans say the Blackwood has high-level support in the company and could hit showrooms in 1999. The truck's niche would likely net fewer than 10,000 sales a year but would haul in profits similar to the Navigator's \$15,000 gross margin.

Still, observers say the Blackwood is proof Detroit has gone overboard. And they fear it will distract from the \$30,500 Lincoln LS sporty sedan being unveiled Apr. 7. Gripes one Lincoln dealer: "Navigator elevated the brand and, in one fell swoop,

this will make it a Jay Leno punchline."

Lincoln officials contend they need to take chances—as they did on the Navigator. "Each risk that pays off leads to even more successful risk-taking," says James G. O'Connor, vice-president of the Lincoln-Mercury Div. But will the Blackwood prove worth the risk?

By Keith Naughton in Detroit

WHEEL LUXURY

The Blackwood would have a Lincoln Navigator grille and a leather-and-burled-walnut interior



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EDITED BY KELLEY HOLLAND

A BLOOD SUBSTITUTE GETS BLOODIED

NOT SO FAST: BAXTER INTERNATIONAL ended a late-stage patient trial in the U.S. of its HemAssist blood substitute when it discovered that trauma patients given the product in the hospital were dying at a rate greater than a control group and even higher than normal mortality rates. But Baxter believes the product can still work when administered to patients earlier in their treatment. So it is continuing trials in Europe on trauma patients who would be given HemAssist in the ambulance following a major car accident or gunshot wound, and in the U.S. on patients undergoing elective surgery.

Officials expect to have HemAssist on the market by late 1999 or early 2000. Sanford C. Bernstein analyst Kenneth Abramowitz figures that the market may now be 25% smaller than the \$2 billion to \$4 billion he had expected.

POWER RESURGENCE AT CABLETRON

CRAIG BENSON JUST WASN'T ready to fade away. On Mar. 30, the Cabletron Systems chairman pushed aside his handpicked successor and reassumed control of the networking company he co-founded. The move came a week after Cabletron posted its first-ever quarterly loss, of \$6.3 million. While praising CEO Donald Reed's strategic skills, Benson told analysts, "I can make smart decisions and implement a lot faster than he possibly could." Still, some expect tough times ahead. "What Cabletron really needs is a new culture," says David Passmore of NetReference. Maybe one with less hubris?

LAZARD'S EXIT DOOR IS REALLY SWINGING

STEVEN RATTNER, THE deputy chief executive of Lazard Frères, hasn't had much luck holding on to all his top talent. In recent weeks, three senior bankers have bailed out. Gerald Rosenfeld, who was Lazard's head of investment banking, departed to join NationsBanc Montgomery Securities; Kendrick Wilson III, a managing director in the financial services group, joined Goldman Sachs; and Ira Harris, a senior banker in Lazard's Chicago office, went to work for the Pritzker family. "This is a firm with 1,200 people and 70 partners," says a senior insider. "There's a generational change going on."

HEADLINER: IRA MILLSTEIN

CORPORATE AMBASSADOR TO THE WORLD

Ira Millstein is packing up his corporate governance principles and taking them on the road. The governance maven and senior partner at Weil, Gotshal & Manges is leading a group that on Apr. 2 gave the Organization for Economic Cooperation & Development a set of recommendations that could dramatically change how non-U.S. companies are governed.

The report calls for smaller, more independent boards and argues that a company's central mission should be creating shareholder wealth. These aren't radical notions in the U.S.,

but they're a sharp departure from practices overseas. In Japan, boards are almost exclusively made up of insiders; in France, companies believe their commitments to employees and society are every bit as important as their responsibility to shareholders.

Assuming the OECD ministers approve the report, they'll urge companies to get on the bandwagon. But will the reforms take? Many management experts outside the U.S. are skeptical. That leaves investors to demand the same things they do in the U.S.

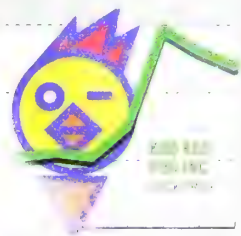
By John Byrne



CLOSING BELL

LEE IAKOOKOO

Koo Koo Roo was crowing on Mar. 30. The Los Angeles-based restaurant operator said Chairman Kenneth Berg would step down for health reasons and be replaced by none other than Lee Iacocca. Word of the ex-Chrysler chairman's involvement sent the stock up 72%, to 3%. As acting chairman, Iacocca is said to be working with new CEO William Allen on restructuring Koo Koo Roo, which operates 38 chicken eateries and 14 Hamburger Hamlets. But Wall Street's elation faded: By Apr. 1, the stock settled at 2 2/3%.



APR. 1

MARKET

ZENITH MAY BE AT ITS NADIR

THE PICTURE IS DARKENING at Zenith Electronics. On Apr. 1, it reported its ninth straight annual loss, \$299 million, and warned of possible bankruptcy without a major cash infusion or new partner. The stock fell 31%. Some \$45 million in secured credit through June 30 was extended by controlling shareholder LG Electronics of Korea. But Zenith needs at least \$225 million to get through the year. New CEO Jeffrey Gannon, who came from General Electric in January, plans more cost-cutting soon, but it's unclear how long LG will hang on.

ARE MOVIE TICKETS TOO CHEAP?

DOES EDGAR BRONFMAN JR. need a remedial class in economics? The CEO of Universal

Studios owner Seagram startled a media confab on Mar. 31 when he said the movie industry should charge more for movies that cost more to make. Current pricing, he said, "makes no sense and I believe the entire industry should and must revisit it." The idea was so far-fetched that some think he misspoke. "I'm sure he didn't mean that," says Bob Goodrich, president of Goodrich Quality Theaters. Bronfman was unavailable for clarification.

ET CETERA...

- CompUSA told investors that third-quarter profits would be below expectations.
- Johnson & Johnson won FDA approval for Sucralose, a no-calorie sweetener.
- Mañana: MCI, arguing with the SEC about fourth-quarter charges, will file a 10-K late.
- Ian Schrager has teamed with private REIT NorthStar Capital to develop hotels.

EDITED BY DOUGLAS HARBRECHT

WILL TONS OF HIGHWAY PORK LATTEN THE BALANCED BUDGET?

President Clinton's coming showdown with Congress over a \$217 billion highway bill promises to be more than a punch-out over pork-barrel projects. In many ways, it will be a defining moment of his second term. If the President doesn't take a stand against runaway transportation spending, he'll soon find his long-sought balanced budget bill over. And he'll send a message to Hill porkmeisters that the coming era of budget surpluses gives them license to spend like drunken swabbies.

The six-year highway and transit measure that's pending for overwhelming House approval would increase transportation spending by \$33 billion above levels of last year's budget accord. Republican leaders have let the bill's drafters salt it with 1,467 "demonstration projects"—\$9.3 billion targeted for new roads, bridges, and even university studies in 100 congressional districts.

MUSCLED. So what happened to the GOP's famed fiscal discipline? The party is nervous about losing control of the House in November, and bringing home the bacon is a sure voter-getter. Democrats are happy to play along—they get their cut. And House Transportation Committee Chairman Bud Shuster (Pa.), the Hill's Prince of Pork, outmuscled fiscal hawks like House Budget Chairman Dan Rostenkowski (R-Ill.), who says the bill perpetuates Washington's "culture of spending." House GOP leaders swear they'll honor the balanced budget deal, promising to make offsetting cuts in other domestic programs. But budget experts wonder how real any cuts of that magnitude would be. "They're going to cut the caps, either explicitly or by subterfuge," says former Congressional Budget Office Director Rudolph G. Penner. Although Administration budgeteers are clucking over the bill's edifice complex, Clinton isn't exactly a fiscal purist himself. His 1999 budget calls for a \$90 billion increase in do-

mestic spending, much of it for education and other "public investments." Now he fears that Congress' love of asphalt and buses will come at the expense of his social agenda.

But a frontal assault on Shuster's bill would inflame congressional Democrats—dangerous for a President still under the threat of impeachment. So Clintonites are joining with

Kasich and moderate Democrats to create enough embarrassment to whittle the bill down in negotiations with the Senate.

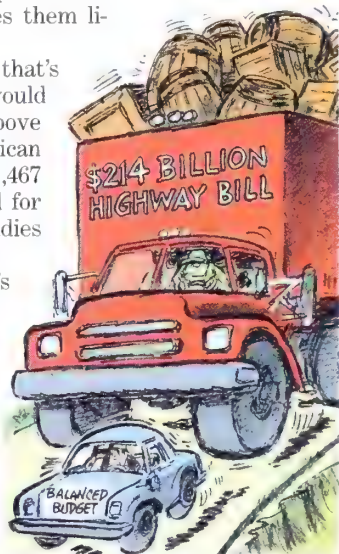
BARGE BOONDOGGLE? Shuster & Co. will counter that public-works spending packs a mighty economic wallop—creating jobs and paving the way for a more productive economy. Even after a big spending boost in 1991, the U.S. needs to pour \$358 billion into roads and \$73 billion into transit between now and 2002 to keep traffic moving, argues the American Association of State Highway & Transportation Officials.

But with the economy running at top speed, public-works stimulus is hardly vital. As for boosting productivity, "infrastructure is important, but it's not special," says economist Douglas Holtz-Eakin of Syracuse University. Transportation spending looks even worse when the cash is earmarked by politicians—a practice the House is taking to record levels. Two examples: \$14 million to buy barges for a company that transports new cars to dealers in Brooklyn and Manhattan and \$2.75 million

for an access road to a Dayton baseball stadium.

Largesse like that buys loads of support on the Hill. That's why White House aides consider the threat of a Presidential veto, as one puts it, "mere symbolism." They hope Clinton can schmooze the bill down till it's closer to \$200 billion. But it's hard to negotiate over the roar of a bulldozer.

By Mike McNamee



GOP BACON: A sure vote-getter

CAPITAL WRAPUP

STARR'S PAULA PROBLEM

Independent Counsel Kenneth W. Starr is starting to feel like the loneliest man in Washington. U.S. District Court Judge Susan Webber Wright's April 1 bombshell, tossing out Paula Jones's three-year-old sexual harassment lawsuit against Bill Clinton, is more than a stunning victory for the White House. It could further undermine Starr's efforts to pin obstruction of justice charges on the President. Jones's pursuit of Clinton was "always a weak case," says NYU law pro-

fessor Stephen Gillers. Technically, Starr's case is unaffected—he had no real interest in whether the President engaged in a pattern of abusive sexual behavior—but the Jones upset could leave him on shakier legal ground.

Starr's position already was weakened by Wright's February ruling that allegations Clinton urged former White House intern Monica S. Lewinsky to lie under oath could not be included in the Jones matter. Now, Starr must show that the President obstructed justice in a case that has evaporated.

But Starr's biggest problem is politi-

cal. Starr is expected to deliver his findings later this year to the House of Representatives, which is already planning for possible impeachment proceedings. Now Hill Republicans have to consider the increased political risk to themselves if they launch proceedings that the public sees as a partisan witch-hunt. Starr could still find a pattern of obstruction of justice. But with Clinton on a roll, fewer and fewer Republicans will want to handle the hot potato that Starr lobbs their way. The result: more pressure for Starr to head home.

By Paula Dwyer

Living with heart disease

How do we help people living with heart disease?

At Novartis, the world's leading Life Sciences company, we are developing treatments to help people suffering from hypertension and to reduce the risk of heart attack. Thanks to a treatment from Novartis,

Rita Minard of Williamston, Michigan leads an active retirement with her husband, enjoying brisk walks through the countryside knowing that her medication reduces the risks associated with heart disease.



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MEXICO

HOLDING OFF ASIA'S ASSAULT

So far, Mexican exporters are proving themselves worthy warriors, using close U.S. ties to lock in deals

In the wake of Asia's crisis, pessimists painted a gloomy scenario for Mexico. Asian countries, exporting their way out of recession, flood the U.S. market with cheap goods and grab vital market share from Mexican products. Mexico's three-year export boom fizzles, putting its vulnerable economy in a severe bind.

Well, guess again. Mexican exporters are holding their own north of the border, and even making gains. Sales to the U.S., which takes more than three-fourths of all Mexican exports, rose to \$7 billion in January, up 12.6% over the same month in 1997. The Asian crisis, it turns out, is the key test highlighting Mexico's spectacular export performance under the four-year-old North American Free Trade Agreement (chart).

What the trade deal has locked in place is a hard-to-beat pattern of North American production in which Mexico provides not just cheap labor but also fast delivery and low transport costs. "NAFTA has created durable, long-term relationships between Mexican exporters and U.S. buyers," says Mexican Trade Secretary Herminio Blanco.

Proof of that can be found in Guadalajara. At first glance, its electronics and electrical equipment makers would seem to be prime candidates for battering by head-on competition from Asians. But California's Hewlett-

Packard Co., for example, is shifting contract work to Guadalajara from manufacturers in Asia to supply the U.S. "The market has regionalized into Asia, Europe, and America," says Jaime Reyes, director of HP de México's manufacturing and design center in Guadalajara. "The base of suppliers here in Guadalajara gives us long-term security." HP expects exports to the U.S. of its copier products to reach \$400 million this year, up 25% from 1997.

The same goes for IBM de México, which is pushing its Asian suppliers to set up joint ventures in Guadalajara. "We reduce the cost by producing in Mexico, and we eliminate inventories,"

says Alfonso Alva, director of IBM's Guadalajara plant, which assembles laptops, desktops, and hard drives. Philips Consumer Communications, which employs 7,300 in its Guadalajara plant, exported telephones, answering machines, and pagers worth \$274 million in 1997 and expects a new line of phones to lift sales to \$617 million in '98.

While Mexican exporters are looking strong so far, inroads by Asians can't be ruled out. A study by the Institute of International Finance, a Washington-based research arm of the

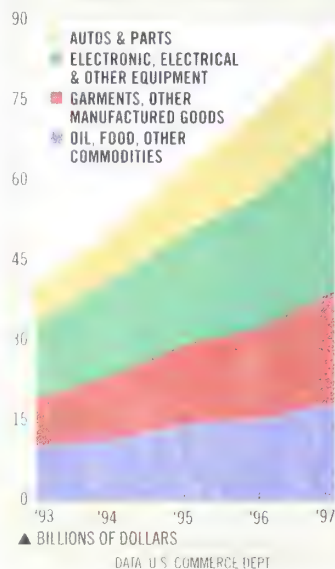


GUADALAJARA WIRING: Philips sees its answering-machine sales rising in '98.

U.S. banking industry, estimates that the Asian crisis could cost Mexico as much as \$5 billion of its exports to the U.S., which totaled \$86 billion last year. But even the study notes that the credit crunch in Asia and Mexico's close U.S. ties will make it hard for Asian producers to take business from Mexico. **OVERTAKING OIL.** A key insulator for Mexico against Asian competition, says Gray Newman, chief Latin economist for HSBC Securities Inc. in New York, is the vast network of almost 3,000 assembly plants, known as *maquiladoras*, that exported goods worth \$41 billion last year, mostly to the U.S. *Maquiladora* products "are an integral part of the manufacturing process" in North America, he says.

One example: Elamex, a contract manufacturer in the border city of Ciudad Juárez. It shipped \$132 million in electrical parts to the U.S. in '97. Long-term contracts—essential to the business—depend on Elamex' closeness to U.S. customers, who can quickly fly engineers down to make changes. "We try to operate as though the border doesn't exist," says Treasurer Jorge Torres.

WHAT'S DRIVING UP MEXICAN SALES TO THE U.S.



The *maquiladora* system also shields huge consumer-electronics industry at the U.S. border. Last year, Mexico exported \$3 billion in TV sets. "When you take into account the freight costs, we're still very competitive" against Japan, says Juan Manuel Hernández, controller of Tijuana-based Sony Mexico Manufacturing Center, which shipped billion worth of TV sets and other products to the U.S. last year.

Even more insulated from Asian competition is the auto industry. Passenger-car exports to the U.S., worth \$8.2 billion last year, have overtaken oil as the leading export north of the border. Atulius Corp., which supplies suspension components to Detroit carmakers, executives are unconcerned about Asia. Samsung gets a lift from NAFTA, which allows duty-free exports within the bloc if at least 50% of a car's components are made in the three NAFTA countries. But Atulius isn't counting just on NAFTA, says Héctor Amador, investor-relations director. "The Big Three don't want inventories," says Amador. "You're practically supplying by the day."

BEYOND NAFTA. Now, Mexican producers are challenging Asia's longtime strength in textiles and even garment-making. By eliminating quotas on garments produced with North American fabric, NAFTA has turned Mexico into the world's leading exporter of clothing to the U.S. The whole industry has been reconfigured," says Salvador Lozano, planning director at Compañía Industrial de París, which sold \$108 million worth of denim in the U.S. last year. "We're so close to the customer. We can fill deliveries. We know the market." Still, Mexican exporters are wary of being overconfident. Already, customers are using the threat of Asian competition to squeeze prices. A Japanese buyer recently warned Samsung executives in Tijuana that he could buy speakers more cheaply in Malaysia. "We have to work hard to improve our productivity," says Young M. Kwon, president of Samsung Electro-Mechanics America. Some analysts say competition could heat up further, especially in products where Asian countries have a technology edge.

But even pessimists can't deny Mexico's newfound export power. The next step: turn this manufacturing strength into markets beyond NAFTA. Ignacio Rivero's small specialty chemical manufacturing company, Tekchem, buys raw materials in the U.S. and sells to European as well as U.S. customers. "We have learned to be efficient," Rivero says. It has taken a crisis on the other side of the world to prove him right.

By Elisabeth Malkin in Mexico City

RUBLES? WHO NEEDS RUBLES?

The virtual economy hides a lot of business—and tax revenue

Russia's Yamal-Nenets Autonomous Region, north of the Arctic Circle, is rich in natural gas, vast in size, and small in population. The local government in the capital of Salekhard gets most of its income from energy royalties. Airplanes are the preferred method of travel. But the tale of how Yamal-Nenets Governor Yuri V. Neyolov acquired a Tupolev 154 airplane shows just how far Russia still has to go be-

gas paid to his government in lieu of energy royalties (chart, page 46). The deal involved not only monopoly Gazprom, which owed the royalties, but manufacturers of aircraft and components in three other cities. The middleman earned a commission—in goods—equal to 10% of the \$17 million plane.

Russia's economy revolves around such deals. They are, in effect, the tape and wire that keep the \$425 billion econ-



fore it can accurately be called a free-market economy.

To get his plane, Neyolov had to turn to what is fast becoming known as Russia's "virtual economy." Representing as much as two-thirds of all transactions in Russia, the virtual economy is a vast web of barter, promissory notes, tax offsets, and other nonmonetary forms of payment. The key players are not banks but thousands of intermediaries called barter specialists. Their job: to put buyers and sellers of goods together, often via complicated chains of transactions. Through such a middleman, Neyolov "bought" his plane by trading

money together despite liquidity shortages and a scarcity of bank credit for companies that can't afford to borrow at Russia's 30% interest rates. Because of barter, scores of enterprises that would have been bankrupt in the West are still producing—and employing workers. That has provided a safety valve, especially for one-factory towns. And because so much business is done with hard-to-measure substitute money rather than cash, official statistics understated the plunge in the economy from 1992 to 1996—and the speed of growth today. The government says Russia's gross national prod-

uct rose 0.4% last year, but the economy may actually be chugging along at 3% or 4%, says Andrei Volgin, president of Moscow-based Adamant Financial Corp.

That doesn't mean barter is a good thing for Russia's economy. With so little business done in cash, the government can collect hardly any taxes. Meanwhile, barter raises the cost of doing business, most economists say. Since most sellers prefer cash, they charge a premium to accept bartered goods or promissory notes. Then, barter specialists take commissions. Together, these markups can add 10% to 70% to the cost of a transaction.

Barter may also be massively distorting the value of Russia Inc. Most companies accept more than half of their revenue in bartered goods. These sales are recorded as inventories, works-in-progress, or accounts receivable. Profits are almost impossible to measure, since the value of a truckload of widgets in lieu of payment in rubles may be arbitrary. Says Volgin: "Corporate books have almost nothing to do with reality."

Why do companies use such a cum-

sory notes also wreak havoc with the Central Bank's monetary policy. They are a form of private money not measured in statistics. Indeed, some experts say that just as much of this substitute money floats around as there are rubles in circulation—some \$61.6 billion. So while the official inflation rate has fallen from an annual 840% in 1992 to 11.4% in 1997, hidden inflation is probably higher.

The barter boom took Boris Yeltsin's government by surprise. His reformers thought that freeing prices in 1992 and later tightening monetary policy would force inefficient enterprises out of business. But companies continued to ship to one another. Those that couldn't pay simply swapped products. In 1994, after the government cut off subsidies, enterprises began issuing promissory notes. These circulate through a large but unregulated market dominated by local banks. Most notes end up in the hands of customers, who return them to the issuing company in exchange for goods or services. A small percentage are redeemed for cash.

Ironically, the government has con-

BUSINESS IN A CASH-STARVED ECONOMY

PORTION OF SALES FOR BARTER



DATA: RUSSIAN GOVERNMENT, ADAMANT FINANCIAL CORP.

1998 budget that aims for a deficit to low 4.7% of GDP. And tax offsets were outlawed as of Jan. 1, 1998. That means all taxes must be paid in cash. In a break with the past, energy giants such as Gazprom and Unified Energy System no longer will be forced to supply government and corporate customers who can't pay. That will minimize the energy trades that are at the root of the barter economy. As Gazprom and its demand payment in cash, Moscow hopes, their customers will begin demanding cash from their own clients.

PAINFUL STEP. Smart managers already are reaping benefits by cutting down on barter. Severstal, a leading steel producer, has cut costs by 10% to 12% since 1996 by paying cash for iron ore, gas, power, and transportation. The company has reduced barter operations from 30% of sales in 1996 to 17% in 1997.

Many more enterprises will have to follow Severstal's lead before the Russian economy can function like a true market. If the government forces more companies to buy, sell, and keep books based on cash, it may sharply accelerate the restructuring of Russian industry. Such steps may prove painful, but they could speed growth and bolster government coffers as companies generate the cash they need to pay taxes.

A big question is whether Moscow has the guts to push through such a strategy just two years before key presidential elections. It faces a difficult task: convincing both voters and the Communist-dominated Duma that keeping the virtual economy alive will, in the end, sabotage workers' security. Barter was an innovative way for companies to survive the initial stresses of the shift to capitalism. But now, the country must trade in its virtual economy for the real thing—one based on cold, hard cash.

By Patricia Kranz in Moscow

PORTRAIT OF A DEAL

1 GOVERNOR of Yamal-Nenets Region demands payment of energy royalties from gas monopoly **GAZPROM**.

2 GAZPROM, claiming to lack cash, offers to pay in gas.

3 GOVERNOR asks barter specialist, **ANDREI TOLMACHEV**, to trade the gas for an airplane.

4 TOLMACHEV then signs contract with aircraft manufacturer **AVIACAR**.

6 GOVERNOR gets his plane six months after the transaction begins. **TOLMACHEV** earns a commission equal to 10% of the \$17 million plane.

5 AVIACAR, lacking cash, can't buy components to make the plane. **TOLMACHEV** trades more than 100 cars, tractors, and buses to acquire a \$2 million engine and swaps \$250,000 of electricity and tires to secure electrical equipment from different companies.

bersome system? For many heavy industries, it's a matter of survival. Machine-tool builders, steel mills, and chemical makers have a harder time selling goods than producers of consumer items, so they rely on barter. For more prosperous companies, barter is a way to skirt Russia's onerous taxes. "Companies report virtual profits and have no cash to pay wages or taxes," says Pyotr Karpov, deputy head of Russia's bankruptcy commission and author of a government study on barter.

Needless to say, proliferating promis-

tributed to the growth of this virtual economy. Under pressure from the International Monetary Fund to cut state spending, Yeltsin's policymakers sometimes substituted tax credits for government outlays. By 1997, only 10% of tax payments were made in cash, says Karpov. The rest came in the form of electrical energy, natural gas, or rail shipments that the government accepted from companies in lieu of cash.

Now, Moscow wants to break the barter chain. After months of resisting, the parliament recently passed a tight

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COMMENTARY

By Dexter Roberts and Pete Engardio

CHINA: FINALLY, A CHANGING OF THE GUARD

It's the kind of publicity whirlwind rarely seen by a Chinese leader. Days after Zhu Rongji wowed Chinese TV viewers with a live press conference, where he joked with reporters and fielded questions on such taboo topics as democracy and the 1989 Beijing massacre, the new Premier was in northern China meeting with suffering blue-collar workers. Then he was off to London. Then Paris. Now, U.S. diplomats are pushing to get Zhu to visit Washington this fall.

That a top official is portraying himself as globally minded and answerable to the public speaks volumes about the new style of leadership emerging in Beijing. Compared with such stodgy apparatchiks as former Premier Li Peng—and especially to the xenophobic Communist Party fossils who reigned just a few years ago—the change is remarkable. President Jiang Zemin, like Zhu a fluent English speaker, charmed Americans last summer with an unscripted question-and-answer session at Harvard University. Such top leaders as Vice-Premiers Li Lanqing and Wu Bangguo and Central Bank chief Dai Xianglong also impress foreign visitors with their detailed, no-nonsense explanations of China's free-market reforms



PEOPLE'S CONGRESS:

A slew of reforms were introduced

and economic problems.

It's more than PR. Behind this new era of frankness is a historic changing

of the guard. With the passing or retirement of revolutionaries such as Deng Xiaoping, Chen Yuan, and Yang Shangkun, Beijing is now dominated by technocrats whose main concern is solving China's many problems. Of the top seven party leaders, five have degrees from prestigious Chinese universities. Jiang and Zhu, aged 71 and 69, are engineers. So is Vice-President Hu Jintao. Three of China's four vice-premiers have extensive economic experience. Below them, younger technocrats—some U.S.-trained—hold high posts in the Finance Ministry, banks, regulatory bodies, and think tanks.

The impact of this generational change already is profound. No longer stifled by a powerful old guard, the leadership is wasting no

time pushing its radical agenda. With Zhu rather than the conservative Li Peng controlling the bureaucracy, a crash plan to overhaul China's financial system, state enterprises, and major ministries is under way. Big foreign investments that have been stymied for years are getting approved. And calls for political reform, muted since '89, are resurfacing. "This govern-

ment is business-oriented," says Fan Gang, director of the National Economic Research Institute. "Instead of talking about principles, they are looking for solutions."

To be sure, Washington and Beijing still have lots of differences. Jiang and Zhu are no democrats. They are unlikely to compromise on Taiwan and Tibet, and they believe the state should retain a big stake in industry. But neither had a hand in the Tiananmen Square massacre. That will make it easier for President Bill Clinton, who will visit Beijing in June, to appear cordial.

Of course, there's still the danger that Zhu's economic reforms will fail and cause a relapse of more central control. Also, branches of government that aren't managing the economy tend to be staffed with political appointees. Take the Supreme People's Procuratorate, China's top crime-fighting agency. The new head, Han Zhubin, is a railways-ministry vet with no legal experience or even a college education. But in the economic ministries, progress will be difficult to undo. "They've gotten rid of most of the incapable people," says Yan Xuetong, a director at a Chinese foreign-policy think tank.

China won't become like the rest of the world overnight. But as power shifts toward these more outward-looking technocrats, the rest of the world should find dealing with China ever more comfortable.

Roberts is BUSINESS WEEK's Beijing correspondent, and Engardio is a senior news editor.

BEIJING'S NEW TECHNOCRATIC ELITE

NAME/AGE/TITLE	BACKGROUND
WU BANGGUO 56, Vice-Premier	A Jiang Zemin protégé who helped oversee development in Shanghai. Responsible for state enterprise reform
LI LANQING 65, Vice-Premier	English-speaking Fudan University graduate who is responsible for trade issues
WEN JIABAO 55, Vice-Premier	The only high official tied to reformist premier Zhao Ziyang in the 1980s. In charge of finance and agriculture
DAI XIANGLONG 53, Central Bank Governor	Liberal reformer who is closely tied to Zhu Rongji
XIANG HUAICHENG 59, Finance Minister	Technocrat who spent 26 years rising through the ranks of the Finance Ministry

DATA: BUSINESS WEEK



How do you measure things like enthusiasm, cooperation and trust?

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Most common side effects with ZYBAN include dry mouth and difficulty sleeping. Although uncommon, there is a risk of seizure associated with ZYBAN. (See Important Warning* section in Information for the

Patient on following page.) So it is important to talk to your health care professional to see whether ZYBAN is right for you. You should not take ZYBAN if you have a seizure disorder; are already taking WELLBUTRIN®, WELLBUTRIN SR®, or any other medicines that contain bupropion HCl; have or have had an eating disorder; or are currently taking or have recently taken a monoamine oxidase (MAO) inhibitor. It is important to let your health care professional know about any other prescription or over-the-counter medications you are taking. ZYBAN is not recommended for women who are pregnant or breast-feeding.

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Please consult Information for the Patient on the following page.

Information for the Patient

ZYBAN™ (bupropion hydrochloride) Sustained-Release Tablets

Please read this information before you start taking ZYBAN. Also read this leaflet each time you renew your prescription, in case anything has changed. This information is not intended to take the place of discussions between you and your doctor. You and your doctor should discuss ZYBAN as part of your plan to stop smoking. Your doctor has prescribed ZYBAN for your use only. Do not let anyone else use your ZYBAN.

IMPORTANT WARNING:

There is a chance that approximately 1 out of every 1,000 people taking bupropion hydrochloride, the active ingredient in ZYBAN, will have a seizure. The chance of this happening increases if you:

- have a seizure disorder (for example, epilepsy);
- have or have had an eating disorder (for example, bulimia or anorexia nervosa);
- take more than the recommended amount of ZYBAN; or
- take other medicines with the same active ingredient that is in ZYBAN, such as WELLBUTRIN® (bupropion hydrochloride) Tablets and WELLBUTRIN SR™ (bupropion hydrochloride) Sustained-Release Tablets. (Both of these medicines are used to treat depression.)

You can reduce the chance of experiencing a seizure by following your doctor's directions on how to take ZYBAN. You should also discuss with your doctor whether ZYBAN is right for you.

1. What is ZYBAN?

ZYBAN is a prescription medicine to help people quit smoking. Studies have shown that more than one third of people quit smoking for at least 1 month while taking ZYBAN and participating in a patient support program. For many patients, ZYBAN reduces withdrawal symptoms and the urge to smoke. ZYBAN should be used with a patient support program. It is important to participate in the behavioral program, counseling, or other support program your health care professional recommends.

2. Who should not take ZYBAN?

You should not take ZYBAN if you:

- have a seizure disorder (for example, epilepsy).
- are already taking WELLBUTRIN, WELLBUTRIN SR, or any other medicines that contain bupropion hydrochloride.
- have or have had an eating disorder (for example, bulimia or anorexia nervosa).
- are currently taking or have recently taken a monoamine oxidase inhibitor (MAOI).
- are allergic to bupropion.

3. Are there special concerns for women?

ZYBAN is not recommended for women who are pregnant or breast-feeding. Women should notify their doctor if they become pregnant or intend to become pregnant while taking ZYBAN.

4. How should I take ZYBAN?

- You should take ZYBAN as directed by your doctor. The usual recommended dosing is to take one 150-mg tablet in the morning for the first 3 days. On the fourth day, begin taking one 150-mg tablet in the morning and one 150-mg tablet in the early evening. Doses should be taken at least 8 hours apart.
- **Never take an "extra" dose of ZYBAN.** If you forget to take a dose, do not take an extra tablet to "catch up" for the dose you forgot. Wait and take your next tablet at the regular time. Do not take more tablets than your doctor prescribed. This is important so you do not increase your chance of having a seizure.
- It is important to swallow ZYBAN Tablets whole. Do not chew, divide, or crush tablets.

5. How long should I take ZYBAN?

Most people should take ZYBAN for 7 to 12 weeks. Follow your doctor's instructions.

6. When should I stop smoking?

It takes about 1 week for ZYBAN™ (bupropion hydrochloride) Sustained-Release Tablets to reach the right levels in your body to be effective. So, to maximize your chance of quitting, you should not stop smoking until you have been taking ZYBAN for 1 week. You should set a date to stop smoking during the second week you're taking ZYBAN.

7. Can I smoke while taking ZYBAN?

It is not physically dangerous to smoke and use ZYBAN at the same time. However, continuing to smoke after the date you set to stop smoking will seriously reduce your chance of breaking your smoking habit.

8. Can ZYBAN be used at the same time as nicotine patches?

Yes, ZYBAN and nicotine patches can be used at the same time but should only be used together under the supervision of your doctor. Using ZYBAN and nicotine patches together may raise your blood pressure. Your doctor will probably want to check your blood pressure regularly to make sure that it stays within acceptable levels.

DO NOT SMOKE AT ANY TIME if you are using a nicotine patch or any other nicotine product along with ZYBAN. It is possible to get too much nicotine and have serious side effects.

9. What are possible side effects of ZYBAN?

Like all medicines, ZYBAN may cause side effects.

- The most common side effects include dry mouth and difficulty sleeping. These side effects are generally mild and often disappear after a few weeks. If you have difficulty sleeping, avoid taking your medicine too close to bedtime.
- The most common side effects that caused people to stop taking ZYBAN during clinical studies were shakiness and skin rash.
- Contact your doctor or health care professional if you have a rash or other troublesome side effects.
- Use caution before driving a car or operating complex, hazardous machinery until you know if ZYBAN affects your ability to perform these tasks.

10. Can I drink alcohol while I am taking ZYBAN?

It is best to not drink alcohol at all or to drink very little while taking ZYBAN. If you drink a lot of alcohol and suddenly stop, you may increase your chance of having a seizure. Therefore, it is important to discuss your use of alcohol with your doctor before you begin taking ZYBAN.

11. Will ZYBAN affect other medicines I am taking?

ZYBAN may affect other medicines you're taking. It is important not to take medicines that may increase the chance for you to have a seizure. Therefore, you should make sure that your doctor knows about all medicines—prescription or over-the-counter—you are taking or plan to take.

12. Do ZYBAN Tablets have a characteristic odor?

ZYBAN Tablets may have a characteristic odor. If present, this odor is not

13. How should I store ZYBAN?

- Store ZYBAN at room temperature, out of direct sunlight.
- Keep ZYBAN in a tightly closed container.
- Keep ZYBAN out of the reach of children.

This summary provides important information about ZYBAN. This summary cannot replace the more detailed information that you need from your doctor. If you have any questions or concerns about either ZYBAN or smoking cessation, talk to your doctor or other health care professional.

GlaxoWellcome

Glaxo Wellcome Inc.
Research Triangle Park, NC 27709

U.S. Patent Nos. 5,427,798 and 5,358,970
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EDITED BY JOHN TEMPLEMAN

WHY THE SAUDIS ARE INCHING AWAY FROM WASHINGTON'S TENT

Shortly after President Clinton's Middle East envoy, Dennis Ross, flew to Israel in late March, the Foreign Ministers of Egypt and Syria were jetting to Saudi Arabia. Despite the different destinations, they all wanted to discuss the same topic: the Middle East peace process, how to get it back on track, and on what terms. It was yet another demonstration of how Saudi Arabia, Washington's staunchest Arab ally, is moving toward an independent foreign policy.

A few weeks earlier, the sudden hospitalization of Saudi Arabia's already frail, 77-year-old King Fahd bin Abdulaziz had underlined that his reign over the kingdom's instinctively pro-U.S. policies are coming to an end after 16 years. While one suggests that Saudi Arabia and the U.S. are on a collision course, the ascendancy of Fahd's half-brother and designated successor, Crown Prince Abdullah, 73, means that the U.S.-Saudi relationship will be "much more complicated" than before, as one top State Department official puts it. Adds Sarah Yizraeli, visiting fellow at the Washington Institute for Near East Policy: "[Abdullah] will decrease Saudi dependence on the U.S."

NEW INITIATIVE. Already, Abdullah has put a long stamp on Saudi foreign affairs. He has engineered the surprising rapprochement between Saudi Arabia and its longtime enemy, Iran. Abdullah, who is related by marriage to the family of Iran's Hafez Al-Assad, Iran's key Arab ally, went to the Islamic summit in Tehran last December. By February, the crown prince was hosting a large Iranian delegation headed by former President Hashemi Rafsanjani—the first high-level Iranian visit to Saudi Arabia since the Shah of Iran's overthrow in 1979. Now, air links between the two countries are resuming after a long hiatus. Some critics charge that Abdullah still is attached to romantic notions of pan-Arabism. Like many other Gulf Arabs,

for example, he helped bankroll Saddam Hussein during Iraq's eight-year war with Iran. But these days, he seems to be aiming for a regional balance of power in which Saudi Arabia plays a pivotal role.

Saudi Arabia's recent actions certainly are at odds with Washington's official policy of dual containment of both Iran and Iraq. Last November, before Abdullah went to Tehran, Riyadh had snubbed a U.S.-sponsored economic summit in Doha, Qatar. More recently, Abdullah seems to have been behind the Saudis' refusal to back a U.S. military strike against Iraq. And some observers detect Abdullah's influence in the pact inked on Mar. 22 in Riyadh between Saudi Arabia, Venezuela, and Mexico to curb oil production—a move that has led to a 27% increase in Gulf oil prices from earlier lows.



ABDULLAH: *Independent*

Although Abdullah's accession to the throne is assured, his leadership of Saudi Arabia still faces some key tests. For one thing, he must manage with great care his relations with King Fahd's six powerful full brothers, particularly Defense Minister Prince Sultan, an erstwhile rival for the succession. The so-called Sudeiri Seven, all sons of the same mother, have long had a monopoly on key government portfolios, such as Defense and Interior—along with the vast patronage and budgets that go

with them. Many Saudis hope Abdullah will crack down on endemic high-level corruption when he succeeds Fahd. Internal change, though, may be slower to come than the shifts in external policies that already are under way. Abdullah is far from being anti-American; U.S. military advisers, after all, helped to train the National Guard that he leads. But his increasing influence will mean a more assertive and more independent Saudi Arabia. And as Washington's Middle East policy crumbles, that will be one more headache for the U.S.

By John Templeman in New York with bureau reports

GLOBAL WRAPUP

SETBACK FOR UKRAINE REFORMS

Prospects that President Leonid D. Kuchma might be able to jump-start Ukraine's crippled economy are considerably dimmer after the Mar. 29 elections. Communists picked up 41 new seats, giving leftist factions more than 170 seats in Ukraine's 450-member Parliament—almost twice as many as moderate pro-reform parties won. The result could doom Kuchma's push to privatize industry, overhaul tax laws, and roll back regulations. Independents, who made a strong

showing, may prove to be a wild card. Many are businesspeople who could support market initiatives. But they're unlikely to form an effective bloc in the fractious legislature, where even pro-reform leaders are squaring off against Kuchma as they position themselves to run in next year's presidential election.

A STRONGER BANK OF MEXICO?

► Mexico may finally take politics out of managing the peso, devalued five times since 1976. A bill sent to Congress by President Ernesto Zedillo Ponce de León on Mar. 26 would give

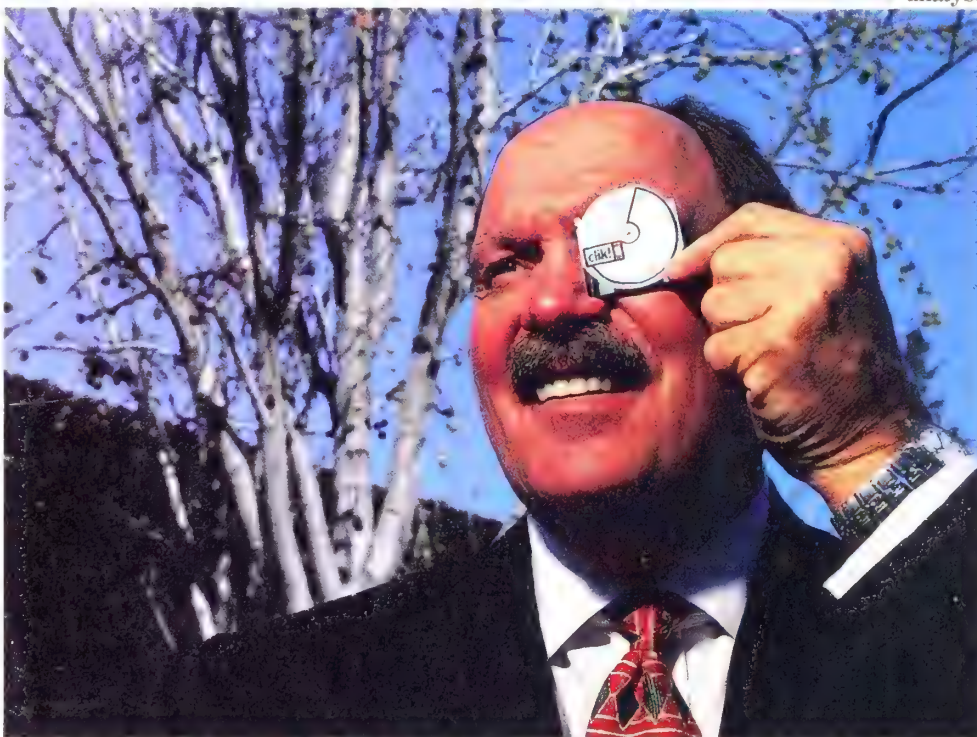
the Bank of Mexico full responsibility for exchange-rate policy. The central bank would also take charge of bank regulation in an effort to halt the lingering crisis in the industry and clean up scandals, such as attempts by drug bosses to muscle into the financial business.

The bank's strengthened powers mean that even if an opposition candidate wins the presidential election in 2000, a Zedillo nominee would continue to run monetary policy. Bank Governor Guillermo Ortiz Martínez started a six-year term in December.

COMPUTER STORAGE

HOW IOMEGA LOST ITS ZIP

Disk-drive sales are flat. Its CEO is out. Can it reboot?



In recent months, enraged customers of Iomega Corp. have been filling homegrown Web sites with angry tales of the “click of death.” That’s the sound that Zip drives, Iomega’s popular computer storage devices, make when they malfunction. But Iomega Chief Executive Kim B. Edwards downplayed the trouble, saying it affected fewer than 1% of Zip drives.

Bad call. The click of death is the sort of operational snafu—along with other production and service lapses—that led to the kiss of death for Edwards. The hard-charging salesmeister—considered by many the top consumer marketer in the stodgy PC peripherals business—shocked the computer industry when he resigned on Mar. 25. “We want to grow this company to \$10 or \$20 billion, not just go to \$3 billion. To do that, you need to do things differently,” says Chairman David J. Dunn, who named director James E. Sierk in-

terim CEO while the company searches for a permanent chief.

Edwards’ fall came even quicker than Iomega’s rise. In just four years since he joined as CEO, Edwards had transformed Iomega from a dying, \$140 million outfit into a \$1.7 billion highflier that grew 43% last year. At its peak in May, 1996, Iomega had a market capitalization of \$7 billion. Today, it’s less than a third that. Now, just three months after the board approved Edwards’ 1998 growth plans and gave him a \$641,000 bonus, he’s gone.

What happened? It’s a classic high-tech story. Edwards simply skimped

OVERDRIVE

Edwards developed the Zip drive in a year of “managed chaos.” But glitches are hurting

on the basics—fine-tuning production and tending to customer complaints—his hurry to put Iomega on the map. Edwards was in many ways a victim of his own success. The more Zip drive consumers snapped up, the more critical became such mundane tasks as customer service and supply-chain management—not his strong suits. “Kim got Iomega to where they are, but maybe it’s not all about flash and sizzle anymore—it’s about reducing scrap and improving manufacturing yields,” says analyst Crawford Del Prete of International Data Corp.

But Edwards leaves at a critical juncture. The company’s goal of establishing the Zip drive as the floppy of the future is far from done. Competition is rising fast. Once moribund Syquest Technology Inc. has sold 300,000-plus of its rival SparQ drive, Sony is set to unveil a Zip-like model, and a consortium that includes Compaq Computer Corp. and 3M spin-off Imation is pushing its SuperDisk technology as the standard for portable computers. “The risks are higher than they’ve been,” says Hambrecht & Quist analyst Todd D. Bakar.

Edwards, an 18-year General Electric Co. marketing veteran, came to Iomega with a bold idea: He figured PC owners

SKEWED VISION? Edwards with *Clik!* drive for camera

frustrated by the slim capacity of floppy disks would buy a \$199 storage device that would let them take up to 100 megabytes worth of files or images with them on a single disk. He set Iomega, formerly a maker of high-end corporate drives, on a crash one-year process called “managed chaos” to develop the Zip drive. A year after it debuted in March, 1995, Zip sales passed 1 million.

To rake in the sales and establish itself before a bigger rival stepped in, Edwards shifted Iomega into overdrive. He admonished Iomega’s production people to keep well ahead of demand by ordering parts in high volumes to meet future demand. And he primed the pump with edgy advertising in national publications, with taglines like “It’s hip; it’s Zip.” His li-



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est salvo: a \$100 million advertising campaign—upping the 1998 budget to \$200 million, double last year's. Iomega has sold more than 12 million Zip drives. And PC powerhouses like Dell Computer Corp. and Compaq now include Zip drives on some of their PCs.

POTHOLES. But Edwards was not able to keep Iomega on the fast track without hitting pot-holes. From the start, the company struggled with suppliers to get quality parts to fill demand—a problem exacerbated when Iomega started up a new factory in Penang, Malaysia, in 1996 without installing up-to-date information systems.

Iomega also couldn't keep up with its growing number of customers. A breach-of-warranty suit was filed last July by angry users, citing long waits for telephone service and hefty charges for the calls. On Feb. 17, the company agreed to settle. Should a federal judge approve the agreement, Iomega will install an online help site, extend warranties for many customers, and pick up \$650,000 in legal expenses.

But the biggest problem of all for Iomega could be quality control. A year ago, the company announced a recall of 75,000 diskettes used with its higher-capacity 1-gigabyte Jaz drive, a follow-on to the popular Zip. That glitch was the result of a bad batch of components. And last December, Iomega delayed introduction of its just released 2-gigabyte version when it became clear the product wasn't performing up to snuff, say suppliers.

As for the Zip, the company insists its quality meets industry standards—but admits that's not good enough to satisfy the PC makers who must bundle it for the Zip to become an industry standard. With PC prices falling to historic lows, computer makers can't risk a wave of returns just to fix a sub-\$100 part. "It's one thing for a consumer to return a Zip drive. It's another to return an entire PC," says Bakar.

Those issues didn't appear to deter Edwards. Analysts say the CEO figured he'd get the chance to plug Iomega's leaks as he pursued his high-speed plans. He had hired former Dell operations boss L. Scott Flaig, who was overseeing installation of software that would help manage production. And di-

IOMEGA'S ROLLER COASTER

JAN. 1, 1994 GE veteran Kim Edwards is hired. With Iomega stock at $\frac{3}{8}$ and sales plummeting, he starts development of a new kind of portable storage, the Zip drive.

MAR. 14, 1996 Thanks to glitzy marketing, Zip shipments reach 1 million and sales more than triple for the year, to \$1.2 billion.

MAY 22, 1996 Urged on by its frenzied Internet followers, Iomega stock hits a high of 27.

APR. 25, 1997 The company recalls 75,000 diskettes for its high-capacity Jaz drive.

OCT. 16, 1997 James Sierk, a retired AlliedSignal exec with a background in total quality management, joins Iomega's board at Chairman David Dunn's behest.

JAN. 25, 1998 Iomega runs a high-priced ad during the Super Bowl—part of Edwards' \$200 million marketing push for 1998.

FEB. 17, 1998 Iomega agrees to settle a class-action suit related to its customer service. Besides setting up a Web site and promising to limit hold times to 10 minutes, Iomega offers toll-free support and extends some warranties.

MAR. 16, 1998 Edwards warns of a first-quarter loss of up to \$25 million on flat sales, sending the stock down 16%, to $7\frac{1}{8}$.

MAR. 25, 1998 Edwards resigns. Sierk takes over as interim chief.

rectors okayed his \$100 million ad campaign at a January board meeting.

But Dunn was growing concerned that the company had outgrown Edwards' go-for-broke style. So when Lawrence A. Bossidy, CEO of AlliedSignal Inc., told him that just-retired Sierk might be looking for a directorship, Dunn invited him to join the board. Sierk, a proponent of Six Sigma quality techniques, accepted in October. He quickly began an informal audit of Iomega's production processes. "Quality is Jim's lifeblood," says Dunn.

Dunn soon had other concerns. After two years of rushing to catch up with demand, sales growth was slowing. Asia's economic woes and soft sales of Zip diskettes hurt revenue. On

Mar. 16, the company said sales would be flat from the year-before quarter's \$360 million. Worse, since these Zip diskettes provide much of Iomega's profits—they carry 50%-plus margins, versus 15% for the \$199 drives—the company expects to lose \$10 million to \$25 million in the quarter that ended Mar. 29.

Company executives say they haven't yet determined the cause of the slow down. But the Asian flu hurt. The company posted \$50 million less than expected in Asia in the fourth quarter, and Iomega Chief Financial Officer Leonard C. Purkis now doesn't expect much sales growth through the first half of 1998.

Push came to shove when revenue growth slowed. Edwards, convinced more marketing could increase Zip drive usage, stuck by his fast-growth plan. The board asked for his resignation, says analysts. Dunn insists that Edwards' departure was unrelated to first-quarter problems. But others don't buy it. "Kim would have been fine so long as there were no execution accidents—but there had a major collision," says J. P. Morgan Securities analyst Daniel Kunstler.

Neither party will discuss details of Edwards' resignation. Says Edwards: "We've had a fantasy run for four years. I'm as proud of our production ramp as any of our marketing."

For Sierk, the solution lies in adding heavy doses of East Coast management theory to Iomega's

West Coast spirit. By tightening requirements on suppliers and improving its information systems, he hopes to avoid glitches. "We have to improve our processes so that everything is not accomplished through heroic last-minute measures," says Sierk.

Will Sierk's textbook approach be enough to establish the Zip as a must-have feature of tomorrow's PC? Company executives insist they're not about to ease up on the gas pedal. "Sometimes when people leave, the course changes 90%. Our course will change 5 to 10%," insists Dunn, who says the plan is to proceed with Edwards' ad blitz until May, when the company will measure the campaign's success. By year-end, the company hopes to hire a new CEO.

He'll no doubt be a nuts-and-bolts executive, but he may need a touch of Edwards' panache, as well.

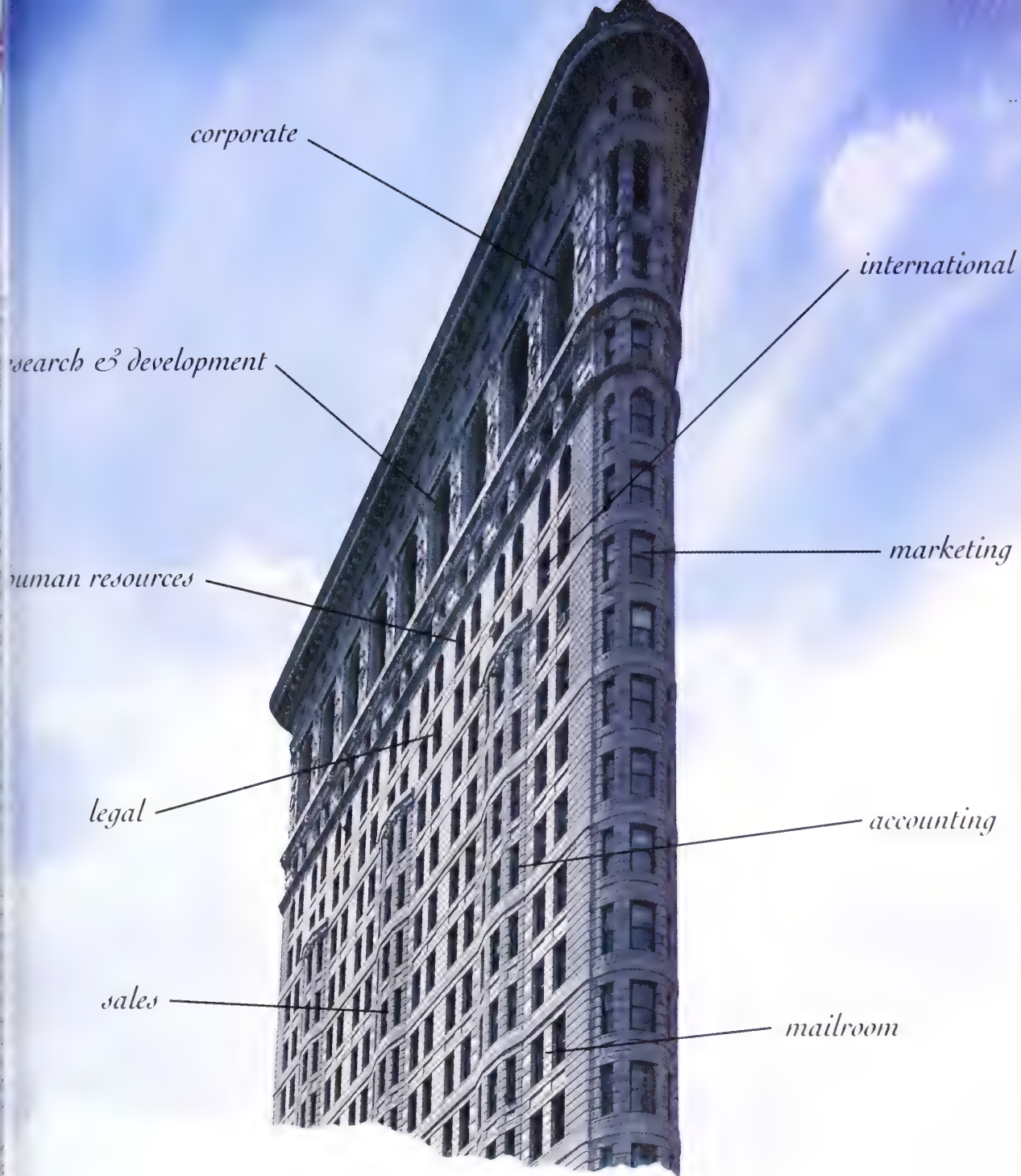
By Peter Burrows
San Mateo, Calif.



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Cutting Fraud, Cutting Costs

DETECTING AND INVESTIGATING FRAUD IS PART OF
CLAIMS MANAGEMENT AT GAB ROBINS

Today, insurance companies and self-insured corporations are stepping up the battle against insurance fraud, spending more than \$650 million per year to combat the problem, according to Mark Stevens, Special Investigations Unit manager at independent claims administrator GAB Robins. Below, this experienced investigator discusses the financial importance of fraud detection and prevention, as well as the impact of new state-level anti-fraud laws.

Q: How large a problem is insurance fraud?

A: Insurance fraud is a tremendous problem. Insurers and self-insureds pay out more than \$30 billion each year in fraudulent claims, according to the National Insurance Crime Bureau (NICB), a Washington-based group.

Q: What is the most common type of insurance fraud?

A: The NICB estimates that between 17% and 34% of all claims reported contain some element of fraud. Although fraud is an issue in all lines, the problem is greatest in workers compensation.

Q: What kinds of fraud do you see?

A: Insurance fraud has become sophisticated. Rings of people move from city to city, employer to employer, setting up accidents and filing claims. In some cases, mills of doctors, attorneys, and claimants are involved in staging accidents. These cases can be much more difficult to unwind, collect evidence on, and prosecute.

Q: Is it true that 'nobody really gets hurt' when insurance fraud is committed?

A: No, absolutely not. Ultimately, the insurance carriers are forced to pass



Mark Stevens,
national manager,
SIU for GAB Robins
North America

fraud costs on to consumers and corporate customers in the form of higher insurance premiums. For companies that self-insure, the cost of fraud is borne directly. In either case, the expense of fraud negatively impacts every company's profits.

Q: Aren't state governments getting involved in the war against insurance fraud?

A: Today, 12 states require insurers and self-insureds to file formal plans to combat fraud with the government. Eleven states also require insurers and self-insureds to have special investigations units (SIUs) to combat fraud. Twenty-three states require fraud warnings on a variety of documents. And 35 states have mandatory fraud reporting requirements. These new requirements are already helping insurers and self-insureds to reduce losses due to fraud. But complying with these new regulations can require the know-how that only experienced fraud investigators and fraud-oriented claims handlers have.

Q: How can insurers and self-insureds reduce fraud and fraud's financial toll?

A: First of all, careful claims management can improve early fraud detection.

Second, special investigations units, composed of seasoned professionals—the kind of people who can spot a stage slip-and-fall a mile away—are invaluable. Within GAB Robins' SIU group, for example, management and investigators have, on average, 15 years of experience in the insurance and/or law enforcement industries. Our SIU team works hand-in-hand with claims management to detect suspicious claims. Also, we help make sure that insurers and self-insureds are in compliance with new government requirements.

Q: Does anti-fraud vigilance pay off?

A: Absolutely. For example, investigation into one auto liability claim revealed that the driver of the car had false identification and had filed many such claims before. The insurer saved nearly \$60,000.

In another incident, a clothing store owner demanded \$287,000 in water damage stock loss and business interruption claims until it was uncovered that he had intentionally staged this and other similar losses. Not every claim investigation turns up such savings, of course, but we estimate overall savings of six times

STATES REQUIRING FRAUD PLANS OR SIUs (YEAR-END 1997)

• ARKANSAS	• KENTUCKY	• NEW YORK
• CALIFORNIA	• MARYLAND	• PENNSYLVANIA
• COLORADO	• MINNESOTA	• TENNESSEE
• FLORIDA	• NEW JERSEY	• WASHINGTON

the cost of investigation. And over the long term, such vigilance will make people think twice about committing fraud—both big scams and so-called white-lies—in the first place.

Clara Van Hast, a New York-based writer reports frequently on insurance and risk management.

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COMPUTERS

HOW THE 'PC KILLER' WAS HUMBLLED

As machines and cheap rivals undercut network computers

When Otto K. Folprecht first heard about slimmed-down desktop machines called network computers two years ago, he was jazzed. The information-systems manager at steel-ducts maker Tree Island Industries in Vancouver, B.C., hoped to slash computing costs 30% by replacing as many as 400 PCs with simpler, cheaper machines from Sun Microsystems Inc.

plans to use NCS. Some, such as Wyse Technology Inc., gave up and switched to making Windows-based terminals. Oracle's Network Computer Inc. unit, which designed the original NCS, laid off 15% of its 200 employees in December and replaced its CEO in February. The rest, including Sun and IBM, sell NCS largely to replace cheap terminals.

What went wrong? Almost every-

change software. "We want the Windows applications," insists Timothy T. Albrecht, information-systems manager at industrial-supplies distributor Fastenal Co. in Winona, Minn., which is using Windows terminals.

The biggest blow to NCS, though, was dealt by the PC crowd. Last year, computer prices sank 40%, to \$1,169 on average, with some PCs edging below \$1,000—smack into NC territory. Meanwhile, Microsoft and Intel Corp., after initially deriding the NC concept, jumped in with promises of cheaper, more flexible ways to manage PCs. In June, Microsoft plans to ship Windows Terminal Server, which will let terminals and PCs run Windows programs from a server. Analysts estimate that the overall cost of a Windows terminal is 25% less than a Windows PC—including maintenance costs—and close to the 30% savings on an NC.



FEATURE: Its But after more than a year's delay, he ditched Sun and bought terminals running Microsoft Corp.'s Windows programs off a central computer. Says Folprecht: "I would have hoped for something from Sun a lot sooner."

BUGS. So had a lot of others. Now, though Sun finally shipped its \$699 iStation NC on Mar. 24, the NC's future looks grim. For a device that Oracle Corp. CEO Lawrence J. Ellison extolled as a PC killer when he conceived it in October, 1995, the dive is breathing. Market researcher Dataquest estimates that 144,000 NCS were sold last year, way off its 400,000 original forecast.

High-profile backers such as Federal Express Corp. have delayed or scrapped

thing. For one, Ellison promised too much too soon. He predicted that NCS would quickly supplant PCs. The idea behind NCS: They would run "applets"—small programs based on Sun's Java network software—that are downloaded on demand from a central server computer. That way, a network computer wouldn't need a disk drive or the manual software upgrades that drive up the price and maintenance costs of PCs. Yet unlike a terminal, which simply displays programs run on a server, NCS have enough horsepower to run applets themselves.

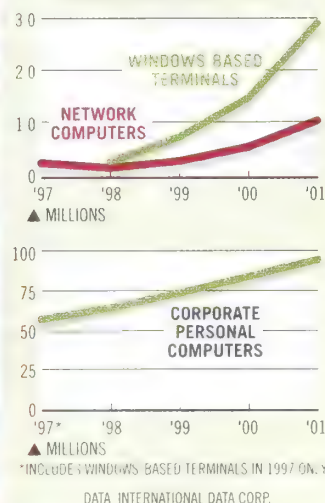
Problem was, because Java was so new, it wasn't ready to do all the tasks customers wanted. Early programs ran slowly and required machines with lots of memory chips—not so slim after all. And companies weren't itching to

The one bright spot in network computers: IBM. In the past year, Big Blue has shipped 100,000 NCS to 3,000 customers including Allstate Corp., which is considering buying as many as 40,000 NCS. IBM's success stems from being one of the first to offer NCS running either Windows or Java programs. Still, with 20% gross margins, they're hardly profit engines. "We got an incredible deal from them," says John Cabral, network manager at Foxwoods Resort Casino in Ledyard, Conn., which is using 650 NCS for jobs like scheduling employees.

Indeed, NC makers may have done little more than goad PC makers into dropping prices. While that's great for buyers, it's cold comfort for NC makers that had hoped to change the computing world.

By Robert D. Hof in Cupertino, Calif., with bureau reports

NCs: A SLOW TAKEOFF WORLDWIDE UNIT SALES



DRUGS

IS GOOD MARKETING BAD MEDICINE?

Why costlier, riskier hypertension drugs are best-sellers

In the treatment of the 50 million Americans with high blood pressure, doctors and cost-cutters line up on the same side: The cheapest antihypertension drugs have been proven in numerous long-term studies to be the safest and most effective. A panel of cardiologists assembled by the National Institutes of Health recommended in 1995 and again last November that, in the absence of other complications, the cheaper drugs should be used. So it seems a no-brainer that doctors in this health-cost-conscious age would rush to prescribe them.

But Alice seems to have stepped through the looking glass. Two new studies show that prescriptions for the cheapest drugs—beta-blockers and diuretics—declined markedly from 1992 to 1996. Meanwhile, prescriptions for the newer and more expensive calcium-channel blockers and ACE inhibitors soared. A 1995 study concluded that overuse of the newer drugs was already adding \$3 billion in unnecessary expenditures to the national medical bill—and the trend is continuing.

ADS GALORE. So what do calcium-channel blockers and ACE inhibitors have that beta-blockers and diuretics lack? Marketing. In the battle for a slice of a \$24 billion market, drug companies are pouring their resources into the higher-priced, higher-profit treatments. Dr. Thomas J. Wang and Dr. Randall S. Stafford of Massachusetts General Hospital reported at the March meeting of the American College of Cardiology that calcium-channel blockers are the most heavily adver-

tised of any drug in the *New England Journal of Medicine*. And it is difficult, they said, to find a single ad for diuretics and beta-blockers (table).

Drugmakers are also dispatching salespeople with pockets full of free

samples. "Virtually every day, my office is inundated by drug-company reps peddling their wares—usually newer, higher-priced medications," says a general practitioner in New York who asked not to be identified. "I do not remember ever—and I mean ever—being approached by a drug rep who was pitching [diuretics or beta-blockers]." This GP says drug reps leave behind stacks of free samples, hoping doctors will give them to patients. "Once a patient is taking medication and it's working well, there's a disincentive to switch to another," he says.

"PUZZLING." The cost implications are huge. A report in the December issue of the *Journal of the American Medical Assn.* (JAMA) estimates that the

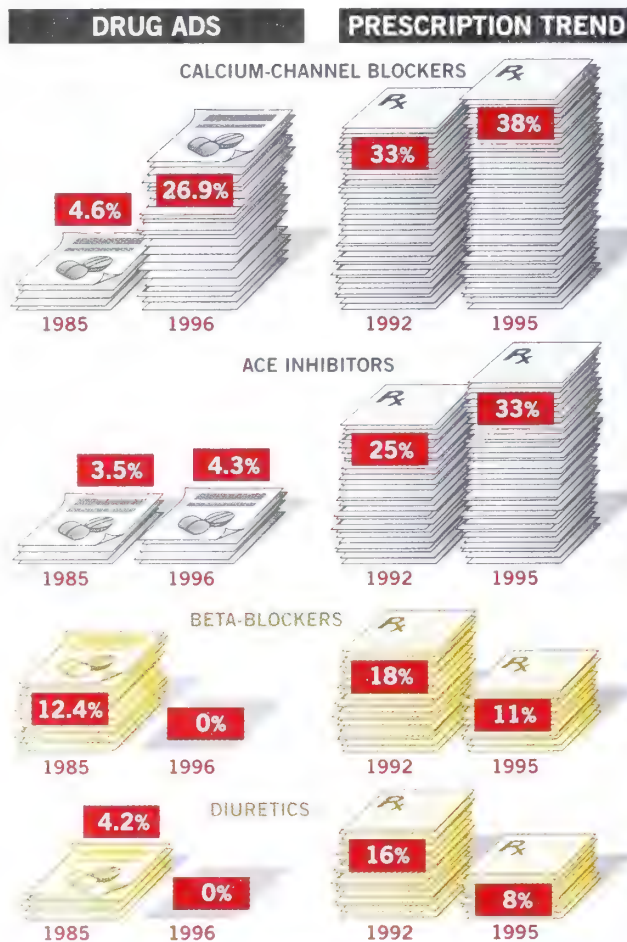
wholesale price of calcium-channel blockers, for example, is more than three times that of diuretics. "I think it's a little bit unfortunate that marketing may influence these [prescribing] trends," says Mass General's Wang. "At a time when we are trying to cut back on health-care costs, it seems a little puzzling that we'd be opting for more expensive medication that we aren't even sure is 100% safe."

In 1995, Pfizer Inc.'s *Procardia*, a calcium-channel blocker also known as nifedipine, was the most prescribed antihypertensive, according to market research firm IMSI Scott-Levin Inc. of Newtown, Pa.; it was the seventh most-prescribed medication overall in the U.S. This is despite the fact that studies have found that calcium-channel blockers are linked to an increased risk of heart attack and cancer—and to a higher rate of suicide. In second place among people with high blood pressure was the ACE inhibitor *Vasotec*, or enalapril, from Merck & Co.

Hypertension drugs first arrived in the 1950s, and they have been remarkably successful. From 1972 to 1994, according to the NIH, approved therapies for hypertension reduced deaths from stroke by 59% and coronary heart disease by 53%. ACE inhibitors and calcium-channel blockers, which arrived in the

DO ADS DISTORT PRESCRIPTIONS?

A higher percentage of the drug ads in the *New England Journal of Medicine* feature costlier calcium-channel blockers and ACE inhibitors over cheaper drugs—beta-blockers and diuretics. The trend in the percentage of hypertension prescriptions for each category is the same. Researchers say there's a link.



DATA: JOURNAL OF THE AMERICAN MEDICAL ASSN., MASSACHUSETTS GENERAL HOSPITAL

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1980s, offered more convenience and fewer apparent side effects than diuretics and beta-blockers. They only had to be taken once a day, for example, while diuretics usually need to be taken three times a day and can cause frequent urination. And beta-blockers sometimes cause fatigue and impotence and can mask signs of low blood sugar.

A decade ago, the National Institutes of Health panel recommended calcium-channel blockers along with diuretics and beta-blockers as the first line of treatment. No large-scale clinical trials had been conducted for the newer agents, so researchers did a new analysis of existing data and found that ACE inhibitors and calcium-channel blockers were no better than the older treatments at lowering blood pressure. And the newer drugs did not reduce the number of deaths.

That was enough to convince the NIH panel. In 1993, the committee changed its guidelines, recommending ACE inhibitors and diuretics—not calcium-channel blockers—be considered the first line of treatment in patients who don't have such complications as diabetes or additional forms

of heart disease. In November, it reconfirmed that recommendation in its sixth set of guidelines.

The change drew criticism from the makers of calcium-channel blockers. "We believe they represent an advance, and we market them based on their safety and efficacy," said Andrew McCormick, a Pfizer spokesman. The questions over the safety of calcium-channel

Calcium-channel blockers are linked to a higher risk of heart attack—and suicide

blockers will not be resolved with any certainty until 2002, with the completion of a large federal trial comparing various hypertension drugs.

In the meantime, doctors seem determined to stay with the new over the tried and true. In the December JAMA study, a team of California researchers reported that in 1995, calcium-channel blockers and ACE inhibitors

made up 71% of all hypertension prescriptions filled by retail drugstores. Beta-blockers and diuretics totaled only 18%. "The role of pharmaceutical promotion practices, including both face-to-face sales activities and pharmaceutical advertisements, probably has had the greatest impact" on prescribing trends, the researchers said.

CALLING ALL GPs. The NIH panel frets that its message on appropriate treatment is just not getting out to the physicians who should be heeding them. Only 53% of patients diagnosed with hypertension receive any kind of treatment. Of those who are treated, most are seen by general practitioners, says Dr. Thomas A. Pearson, chairman of the department of community and preventive medicine at the University of Rochester.

According to the Massachusetts General study, general practitioners are the least likely to prescribe beta-blockers. For these doctors especially, drug companies are a potent source of information, Pearson says. Perhaps managed-care organizations should invest part of their profits in some education of their own.

By Catherine Arnst in New York

INTERNET ADDRESS: <http://www.datek.com>

Business Bulletin

Patho TEK Cures Common Cold

COLD CURE IN A BOTTLE, developed by Patho TEK, is due for release in mid April. CoryzaCC will suppress, and in completely wipe out, all symptoms of the common cold.

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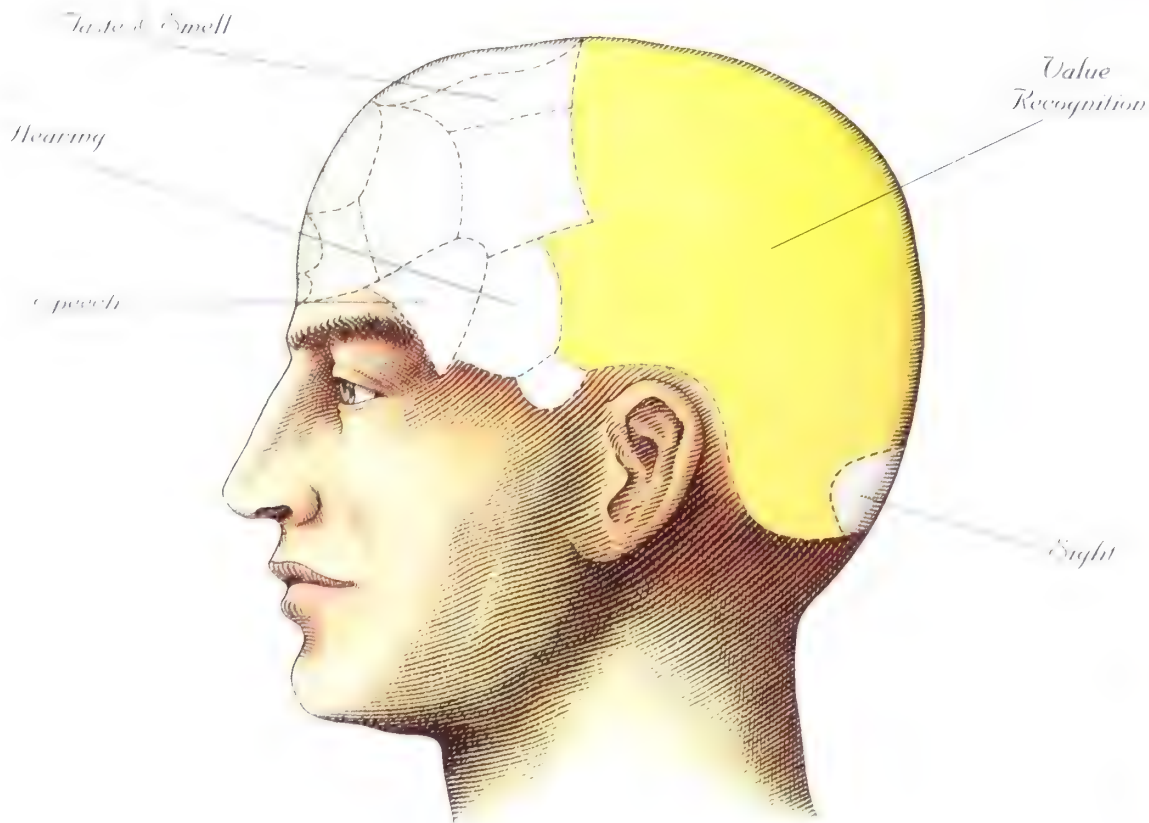


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PAINT THAT SEES JUST BEFORE YOU DO

SPOTTING METAL CORROSION early means that remedial action can be taken before it can weaken a bridge or figure a car. And nowhere is early detection more vital than on aircraft. Now, researchers at Ohio State University have developed a litmus test for structural corrosion—a special paint that visually spots pockets of rust tiny to the naked eye.

Corrosion normally increases the pH, or raises the acidity, of the surrounding metal. So, says S. Frankel, an associate professor of materials science, he blended a paint with naphthalein, a chemical that reacts to increases in pH by turning red. The “litmus test” should be cheaper than the alternative of embedding sensors in a plane’s skin.

Moreover, because the paint can even detect corrosion lurking in the cracks and crannies between metal panels, it promises to minimize the need to periodically take planes apart to check for corrosion. That’s a main reason why the Air Force is funding the research.

So far, though, Frankel and graduate student Jian



Zhang have experimented only with transparent paints. Adapting the concept to pigmented paints “presents lots of practical problems,” Frankel admits. He expects to solve them, but it will take a while. Until then, the paint could be used on interior surfaces. □

EARLY WARNING FOR THE BIG C?

ALTHOUGH SCIENTISTS ARE frantically searching for a cure for cancer, inexpensive tests that detect tumors sooner could provide immense benefits. The sad truth is that in most half of all cases, by the time people learn they have cancer, it’s too late.

Researchers at Johns Hopkins University’s Oncology Center in Baltimore now report preliminary success with a simple saliva test for head and neck cancers. In a report presented to the American Association of Cancer Research meeting on March 1, Dr. David Sidransky said he tried the test on

21 patients already diagnosed with cancer of the mouth or neck. The test was 71% successful in detecting cancer, he said. With 22 tumor-free patients, the test came up 100% negative.

Sidransky’s test looks for evidence of genetic mutations produced in the chromosomes of cancer cells. Spotting these markers in a patient’s saliva, Sidransky says, could cost as little as \$150—and only a few dollars if implemented with microchip-based chemistry. At that point, oral cancer screening could become routine during dental visits. *Catherine Arnst*

HARNESSING NATURE’S CELLULAR DYNAMO

INSPIRED BY PHOTOSYNTHESIS, ENGINEERS LONG AGO devised photovoltaic chips, or solar cells, that convert sunlight into electricity. But plants don’t run on electricity. They rely instead on a special kind of chemical energy using ATP (for adenosine triphosphate) to fuel growth and reproduction.

At Arizona State University in Tempe, chemistry professors Thomas and Anna Moore and Devens Gust are pursuing a new approach to artificial photosynthesis—one that comes a lot closer than solar cells to what plants actually do. They devised a membrane that produces ATP when exposed to light. Their feat is featured in the April 2 issue of *Nature*. The membrane is made from fatty molecules, called lipids, that are infused with synthetic compounds. When these chemicals absorb light, they pump hydrogen ions, or protons, across the membrane and through an enzyme derived from spinach. And this enzyme uses the proton energy to synthesize ATP.

Many hurdles remain before such a device could become useful to industry, including high costs. But someday, a membrane like this could provide energy for the synthesis of drugs or other useful proteins inside artificial cells. “Electrical energy has more than 100 years of history behind it,” Thomas Moore points out. Proton-based energy, in contrast, “is still something that’s unknown outside of living cells.” *Neil Gross*

INNOVATIONS

■ The threat from Africanized “killer” bees might soon be curtailed. An international scientific team has discovered five genes that seem to affect the aggressiveness of Africanized honey bees—and one that may trigger their hyperactive stinging. “We’re still a ways off from being able to stop the spread of the genes,” says team member Gregory J. Hunt, a bee specialist at Purdue University. But breeding programs that spot

■ Budding entrepreneurs in British universities got a \$33 million treat in last month’s government budget. Britain will use the money to set up a



BEE NICE: Research seeks to weed out the “mean gene”

and reject queen bees with the “mean genes” may be possible, he adds. That’s important because domesticated bees pollinate a third of U.S. food crops.

venture-capital fund to finance the commercial development of discoveries by university researchers. Private-sector cash could double the kitty. The initiative was welcomed because Britain’s venture capitalists don’t often back startups. “For too long, the great scientific advances of British universities have gone on to become the manufacturing successes of rival countries,” said Chancellor of the Exchequer Gordon Brown in presenting the budget to Parliament.

I'D LIKE THE WORLD TO BUY A COKE

How Roberto Goizueta
shook up the status quo and
created a global powerhouse

BY DAVID GREISING

In 1954, Roberto C. Goizueta answered a help-wanted advertisement for a chemical engineer in a Havana newspaper and went to work for The Coca-Cola Co. Twenty-six years later, the Cuban-born executive triumphed in a bruising battle for Coke's top job. Named president in May of 1980 and elected chairman and chief executive 10 weeks later, Goizueta had overcome long odds and bested worthy rivals to command one of the world's great enterprises.

But Goizueta could hardly afford to rest on his laurels. The company he headed was mired in a hodgepodge of unrelated ventures, from shrimp farming to winemaking. Its crucial bottler system was badly decayed, with important markets left in the hands of weak operators. There was no strategic vision, and creativity was stifled by a blind adherence to tradition and a refusal to take risks. Worst of all, Coke's stock had fallen by half, and the company was barely turning a profit.

Over the next 12 months, in a period of astonishing activity, Goizueta set in motion a series of initiatives that would



set the course for Coca-Cola for the next 17 years. From the time he became chief executive until his death in 1997, Coke's sales more than quadrupled, from \$4 billion to \$18 billion, while its market capitalization ballooned from \$4.3 billion to \$180 billion, a staggering 3,500% increase. The blueprint for that record—one of Corporate America's best—was largely drawn up during Goizueta's first months in office.

In June of 1980, Coca-Cola Co.'s new president, Roberto C. Goizueta, was eager to get started—to put his mark on the company and pull it into the modern era. Goizueta set out first to cure the soda company's most glaring problem, its troubled bottling system. Next, he would call his managers to Atlanta and purposefully shake them to their roots, questioning every assumption that they held about the business. Only then would Coca-Cola be ready to receive Roberto Goizueta's vision for the future—a vision that respected tradition but held nothing sacred except progress.



Within six weeks of becoming president, Goizueta had a national plan for revamping Coke's network of bottlers. The franchise system of independent bottlers created at the turn of the century had served Coke well, allowing it to expand worldwide with a minimum of capital. But now those operations were in the hands of third-generation owners, many of whom had grown complacent and neglected the capital to keep pace with technology and changes in their markets. Goizueta presented his plan to 15 of Coke's top bottling executives at an all-day meeting in Atlanta. The approach, he explained, would be one of shared responsibility and shared opportunity. The bottlers would have to work hard to improve their relationship—and their businesses. He proposed a more aggressive, focused, and results-driven approach from Atlanta but also decided that the bottlers get tougher, leaner,

and more competitive. "If your sales decline for a single week, we want to know why," he said.

Then, Goizueta unloaded his most dramatic and far-reaching news. It was time to "refranchise" the Coca-Cola bottling system, he said. The company intended to weed out weak operators. Coke's recent purchase of its Atlanta bottler and an investment in its New York bottler were just the start of a broader program of investment. Coke bottlers looking for an exit strategy would find a ready buyer in Corporate Coke, which planned to refurbish weak franchises and put them back out for sale to stronger members of Coca-Cola's system.

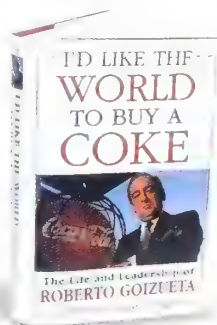
DRAMATIC SHIFT. A stronger bottler system would mean better distribution for Coke as it battled Pepsi in store aisles and soda fountains across the country and would make the bottler's businesses more valuable. It was a dramatic cultural shift for Coke and a signal to the bottlers that Goizueta, whom many had lobbied against in his struggle for the top job, was willing to enter into a new partnership. Ultimately, Goizueta's plan would lead Coke to invest billions as it built the best beverage distribution system in the world.

Bringing new discipline to the bottling system, though vital to Coke's future, was relatively simple compared with the vast cultural changes Goizueta would soon wreak throughout the worldwide organization. But first, he needed to wrest the last remaining power from his mentor, Robert W. Woodruff, the revered former chairman known simply as "the boss," who had saved the company from bankruptcy during the Great Depression and was now its biggest shareholder. Even at age 90, Woodruff was able to use allies on the board and his position as head of the powerful finance committee to retain ultimate control at Coke. Before the Goizueta era could begin, Coke's new leader knew, the Woodruff era had to end.

Goizueta wasted no time. At his first board meeting as chairman-elect in early September, 1980, he made a series of moves that brought the Coke board closer to modern notions of corporate governance and at the same time expanded his authority. First, he imposed three-year terms for board members, eliminating open-ended service. Then, he pushed through a bylaw prohibiting renomination of board members after their 71st birthday, an edict designed to flush out Woodruff and his cronies.

But Goizueta's most important move was to seize control of the purse strings from the finance committee, the vehicle Woodruff had used to exert control over the previous CEO, Paul Austin. To shore up Coke's faltering operations, Goizueta needed capital, particularly borrowed capital. He could not abide the committee's persistent vetoing of pleas to issue debt. And he did not want it to block a plan he was developing to reduce Coke's imprudently high dividend payments.

Goizueta made his move at the September board meeting. Without warning Woodruff in advance, Goizueta proposed adding to the finance committee the company's two top executive officers—himself and, very soon, Coke President Donald R. Keough, Goizueta's most trusted associate. Woodruff missed the September board meeting, and he howled when he heard 10 days later that Goizueta had outflanked him. "Not until today did Mr. Woodruff learn about the



Excerpted from *I'd Like the World To Buy a Coke: The Life and Leadership of Roberto Goizueta* by David Greising, BUSINESS WEEK's Atlanta bureau chief. Copyright © 1998 by David Greising. Reprinted by permission of the publisher John Wiley & Sons, Inc.

action taken," Woodruff's assistant, Joseph W. Jones, wrote to Garth Hamby, corporate secretary. "This is contrary to his concept of the function of the finance committee." But the rules were changed for good and by the spring of 1981, Woodruff would drop off the committee altogether.

The flurry of activity with bottler buyouts and boardroom maneuvering did not mean Goizueta was ignoring the nuts and bolts of the company. During the summer and early fall of 1980, he roamed Coke's headquarters tower, peppering executives with questions in what amounted to a detailed study of every aspect of Coke's business. Goizueta placed special emphasis on Coke's financial intricacies, grilling his subordinates on everything from market size to complex rates of return. Given his lack of sophistication with corporate finance, he was blessed that his predecessors had left him an uncom-

next year's budget. The budget meetings were full of cheerleading, wish lists, and hopeful promises, but there was little hard-nosed planning and almost no accountability.

Goizueta would have none of it. Five-year plans, he felt, were a waste of time. No one could predict with any accuracy what the world would look like in five years. He wanted three-year plans, and he told the executives that he would hold them accountable for meeting their three-year targets. He demanded that managers file their plans early so that he could dissect them. And instead of waiting passively for headquarters to dictate the year's goals, each division chief now had to present his own brief and be ready to defend it. "I want you to tell me what you need to do to expand your business, what kind of capital you need to do it, and what kind of net return you're going to get," Goizueta demanded of Coke's 17 division heads. Mo-



POWER PLAY

After Goizueta (second from right) moved into the top spot, one of his first acts was to dethrone Robert Woodruff (right), a powerful board member and his former mentor

plicated balance sheet, with only \$31 million in long-term debt at the end of 1979. Goizueta knew enough, though, to recognize that he could unlock the power of Coke's assets by leveraging the balance sheet.

"THE SPANISH INQUISITION." As he poked around Coke's executive offices, turning over whatever rocks caught his eye, Goizueta began zeroing in on the areas where he saw weaknesses, especially in the non-soft-drink businesses and in geographic regions where Coke was underachieving. It was all a buildup to the battery of pointed, provocative, and sometimes hostile questions that rained down on Coke's top worldwide executives during a reign of interlocutory terror that became known as "the Spanish Inquisition." To those who had only heard about, but not yet witnessed, the impatient and sometimes even abusive side of Goizueta, the experience was a shock. To those who endured the trial, it was the first concrete sign that their world was about to change forever. Financial results would count above all. And managers would be held responsible for whatever happened on their watch.

The Spanish Inquisition started innocently enough. Coke executives from around the world were accustomed to flying into Atlanta each fall for a two-week business review. There they discussed their five-year plans and were handed a list of objectives that corporate managers had drawn up as their

were sent back to the drawing board to revise their plans.

As Goizueta immersed himself in Coke's budgets, he found that the company's finances were even weaker than he had feared. For years, no one had focused on the cost of capital or the economic return on investments. Handcuffed by Woodruff from borrowing money, Austin had used Coca-Cola stock to fuel an acquisition binge. But due largely to a generous dividend, the company's cost of capital was running about 16 percent per year, more than short-term bank borrowings would have cost in late 1980. Meanwhile, except for soft drinks, none of Coke's businesses—including wineries, water purification, plastics, and foods—were generating more than 10%. "We're liquidating our business, borrowing money at 16 [percent] and investing it at 8 [percent]. You can't do that forever," Goizueta exclaimed.

The horrors Goizueta discovered during the Spanish Inquisition were not limited to Coke's financial mismanagement. Strategically, the company was adrift as well. As he broke down Coke's business into its widespread component parts, Goizueta found there was no coordination, no central planning, no strategic thinking. In Europe alone, Coke was pursuing three totally separate strategies in different countries, pushing packaging innovations in Belgium, extensions of Sprite and Fanta in Germany, and bottling investment in Spain. "This company has no sense of direction,"

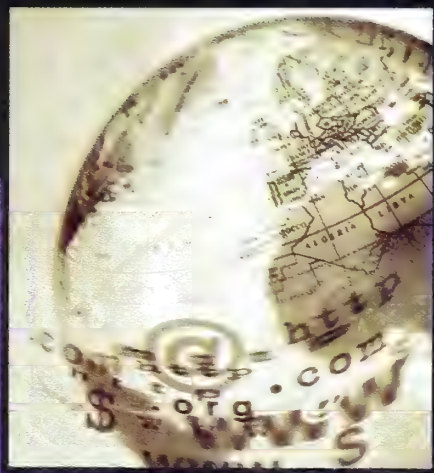
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tion whatsoever," Goizueta declared at one point. "None."

Logical and methodical as ever, Goizueta created a model by which he and his managers could assess Coke's business. Across the top of a sheet of paper, he named the company's operations. On the vertical axis, he listed what he considered the vital financial characteristics of any business: margins, rate of return, cash-flow reliability, and capital requirements. On that basis, Coke's concentrate business—the one on which Woodruff had built the company—proved a winner. Bottling was a little less stellar, but still a solid enterprise. Coke's foods business was further down the line because it ate up huge chunks of capital and was less predictable. Wine, water, and plastics were longshots at best.

At the start of the Spanish Inquisition, Goizueta was shocked to learn how little Coke's managers knew about the financial end of the business—ironically, a criticism that could have been leveled against him just a few months earlier. "None of our operating executives can read a balance sheet," he grumbled. By the time it was finished, he had taken them to school and issued one of the most far-reaching imperatives of his tenure. From that point on, Goizueta warned at one of the closing budget sessions, the corporation would charge its operating units a set percentage for the capital they used. Performance, he declared, would be judged on "economic profit," the unit's operating profit after a deduction for the cost of capital. Strategic planning would be taken seriously, Goizueta said, and objectives would be met. "Don't even come to us with a project that doesn't yield more money than the cost of money," he warned.

FUTURE SHOCK. When the executives limped away from the Spanish Inquisition and returned to their posts around the world, the effect was both immediate and long-term. From Los Angeles to Kuala Lumpur, Coke managers reorganized the way they ran their businesses. They stopped keeping excess inventory of syrup on hand, just in case of an emergency. They quickly switched from stainless steel syrup containers to plastic and cardboard, saving Coke a great deal of money in one blow. They drew up detailed economic models before launching plans for plant expansions or other major investments. "When you start charging people for their cost of capital, all sorts of things happen," said a satisfied Goizueta.

The change of approach was desperately needed. Profits, which had grown 13% a year in the late 1970s, had stopped short, and forecasts showed they would be flat—zero gain—

for all of 1980. The stock market certainly was aware of the troubles. Coke's shares had fallen 50% since their high of \$110 in 1973. Performance in the consumer marketplace was no much better.

To have a lasting impact on the numbers and on Coke's corporate culture, Goizueta realized, he needed to overhaul the way Coca-Cola did business, from the top down. It would be a long and difficult battle to mold Coke into a world-class company at every level. But his job, as he saw it, was to jolt Coke into the future—to shake up the managers and make them understand. The Spanish Inquisition had set the right tone, creating a healthy understanding of the need for change. But without an overarching vision, the revamping would mean anything. The next step was to establish the guiding principles that would carry Coca-Cola through the 1980s, and a blueprint for how to implement those principles.

Two measures would set the process in place. First, Goizueta would create a mission statement for the company. Then, he would gather his top management from around the world and make them sign face to face, to his program. Booklets of principles had a habit of finding their way to bookshelves in managers' offices and staying there, ignored and useless. The following conference would set that from happening. Goizueta would give Goizueta a chance personally to lay down his vision and law.

Goizueta wanted a mission statement to combine a broad vision of Coca-Cola Co. for the next decade with a set of specific strategic steps. He spent weeks bouncing ideas off board members, executives, and consultants—to the point that Keough and others scratched their heads at Goizueta's obsession with such a seemingly in-the-sky project. With great fanfare, he unveiled the result at a board meeting on Mar. 4, 1981. Printed on brown heavy weight paper, it was titled, simply, "Strategy for the 1980s The Coca-Cola Company." Those who took it lightly, did so at their peril. For Coke's new chief, a statement of principles and objectives was a serious undertaking, a compact with the future that he intended to keep.

"Our Challenge," the statement opened, will be to enhance and protect the Coca-Cola trademark, giving shareholders an above-average return and entering new businesses only if they can perform at a rate substantially above inflation. "Our Business," Goizueta wrote, will continue to concentrate in soft drinks, emphasize leadership in our segments, and most likely expand into "industries in which



THE NEW COKE

Goizueta's predecessor Paul Austin (right) was hobbled by the all-powerful finance committee. Goizueta was determined not to meet the same fate

Some people want to extend payment



Other time. Others want a card that will

whatever more

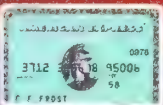
help them do business better. Others



Others want plenty of rewards. It seems



Everybody has different needs, and that's



So we have so many different cards.

do more



Cards

are not today." Only market segments with inherent real growth would be attractive. "Increasing annual earnings per share and effecting increased return on equity are still the name of the game," Goizueta wrote.

The statement concluded with a broad-based section about "Our Wisdom," a set of guiding principles that Goizueta believed would make Coke a leading company as it entered the final decade of the 20th century. As they worked their way into the 1990s, Goizueta wrote, Coke's employees must consider "the long-term consequences of current actions," sacrifice short-term gains when necessary, adapt to changes in consumer tastes and needs, and become a welcome part of every country in which Coke does business. Finally, every Coke employee must exhibit "the capacity to control what is controllable and the wisdom not to bother [with] what is not."

The Spanish Inquisition had proved Goizueta was prepared to launch the kind of guerrilla warfare needed to take Pepsi by the throat, regain leadership in all segments, and squeeze the potential out of the farthest reaches of Coke's vast system. The mission statement showed that Goizueta was also a high-minded corporate philosopher.

Coca-Cola's top managers got their introduction to the mission statement—and to an unambiguous agenda for the Goizueta years—at a conference in Palm Springs, Calif., in April of 1981. It is customary at big companies for new executive teams to invite their elite managers for a retreat, as a way to kick off the new regime. It is not, however, typical to open the session with a harsh kick in the pants, strong enough to shake up even the old-timers waiting to collect their gold watches. But after the Spanish Inquisition, Coke's management corps knew not to expect the predictable from Goizueta. Even so, no one could have anticipated the fusillade that awaited them in Palm Springs.

"NO SACRED COWS." To those who listened, the broad outlines of the Goizueta era were laid out, loud and clear. In his opening remarks, Goizueta announced that a period of rapid change was about to take place at Coca-Cola, and the 40 executives in attendance had better be ready. "Those who don't adapt will be left behind or out—no matter what level they are," he warned. As aides passed out copies of "Strategy for the 1980s," Goizueta warned everyone not to mistake the mission statement for corporate puffery. "Don't take it lightly," he said.

The new chairman made it clear that nothing at Coke

was so sacred it could not be sacrificed for the greater good of the company, and he laid waste to some of Coke's most cherished myths. If Coke's executives wanted to see world-class marketing, he said, they should look at Procter & Gamble Co., not Coca-Cola. The distribution system needed a face-lift. People needed to take bold risks to survive. Combining soda-pop formulas and processing orange juice did not amount to world-class technical strength. And the culture of complacency must change. "The only company that continues to enjoy success is the company that keeps struggling to achieve it," Goizueta said.

Goizueta's concluding passage was filled with portent. "Just to give you an example that there are no sacred cows," he began, "let me assure you that such things as the reformulation of any of all of our products will not stand in the way of seizing a real or perceived market advantage from a competitor." "The days are gone in which an inflexible adherence to a sacred cow will ever give renewed impetus [to] or breathe new life into a competitor," Goizueta swore. In other words, the days of New Coke were not far away.

Though known even within Coke as a hiring and uninspiring speaker, Goizueta galvanized his executives. He built on this by using the five days of the conference to do it, one by one, with every one of his managers. "Now we've got a compact," he would say, after he told him they agreed with his plans. At the conclusion of the conference, Goizueta

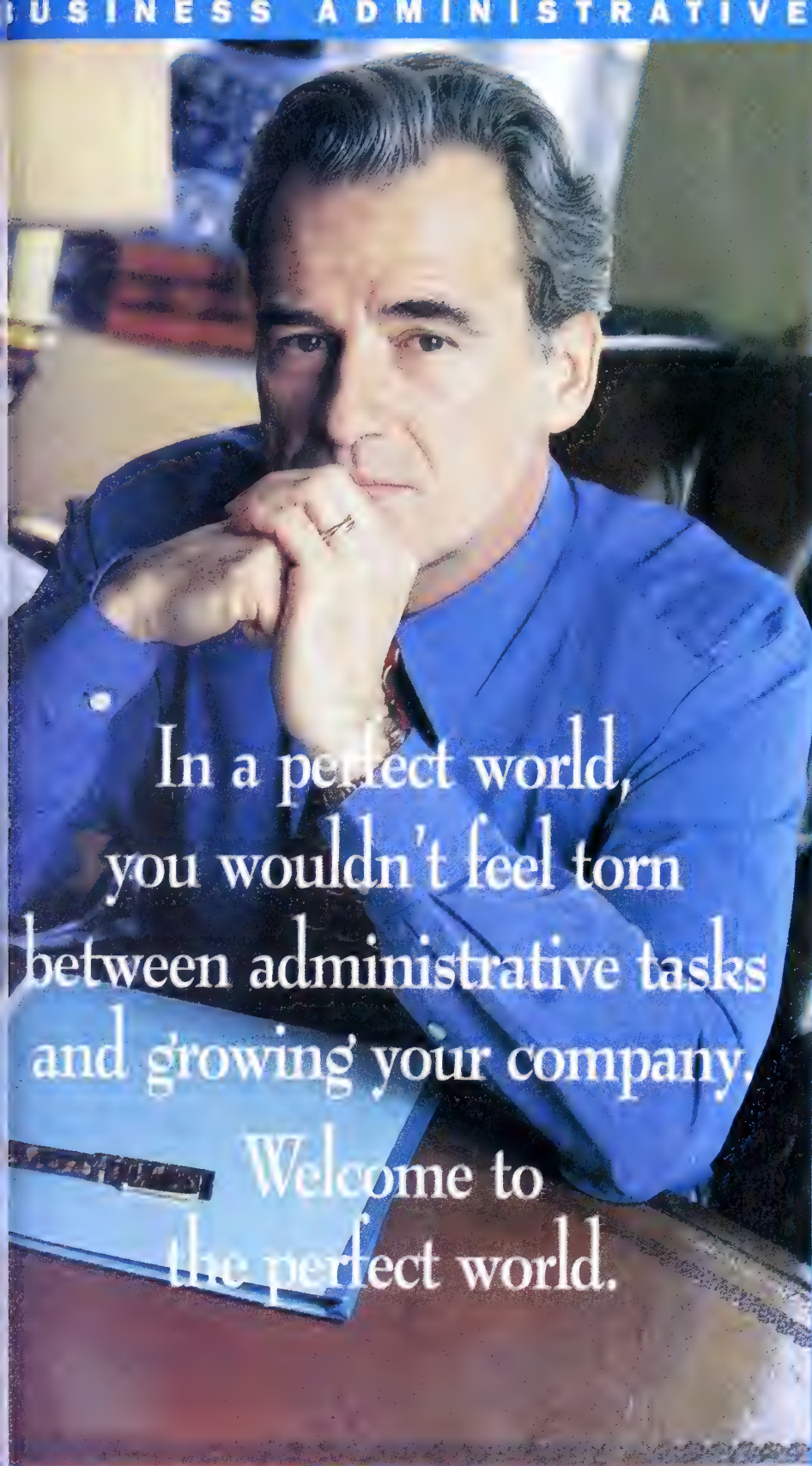


CLASSIC COMBO

Goizueta and Coke President Donald Keough teamed up to drag company managers into a new era, making them responsible for setting their own goals—and meeting them

shared quiet words with the managers as the session broke up. They looked apprehensive, uncertain about the future. When he finished, the chief executive turned to a colleague. "Well," Goizueta said, "we're off to a start."

In fact, the conference in Palm Springs marked a clean break with Coca-Cola's past. But the wrenching changes that Roberto Goizueta imposed in his first year as head of the nation's biggest soft-drink company were just the beginning. Mistakes, such as the purchase of a Hollywood studio and the introduction of New Coke, still were ahead of him, but so were triumphs, such as Coke's invasion of Eastern Europe and the reinvention of Coke's marketing strategies. The basic principles that Goizueta outlined in those early days prepared Coke to rack up one of the most impressive records of shareholder returns in U.S. corporate history, and enabled him to transform Coca-Cola from a sleepy Southern soda maker into a global market powerhouse.



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RIVALRIES

GERMANS IN THE FAST LANE

Mercedes and BMW are gunning for U.S. luxury-car rivals

The U.S. luxury-vehicle market has pretty well stalled these days. Sales are expected to grow a scant 4% over the next two years. But around the New Jersey offices where both Mercedes-Benz and BMW have their American headquarters, optimism reigns. Flush with success from record sales in 1997, the German auto makers are loading up for a product blitz. Mercedes has a flashy new convertible, a souped-up version of its M-class sport-utility, a revamped line of large sedans, and maybe a luxury minivan on the way. BMW is gearing up for the launch of a new version of its popular 3-series sedans this fall, and has a hybrid sport-ute debuting in 1999. "We're going to keep pushing, no matter what," says Victor H. Doolan, president of BMW of North America Inc.

The swagger is back at BMW and Mercedes. It has been a remarkable dual turnaround for the German companies, whose U.S. sales hit rock bottom in 1991 in "We're going to the face of a suc-

BMW'S DOOLAN:
keep pushing"

cessful onslaught by Japanese luxury brands. But they have since left rivals behind in the slow lane. Bolstered by a stable of new products and aggressive marketing campaigns, BMW and Mercedes again rank as the hottest luxury

MERCEDES' JACKSON: A minivan next?

brands in the U.S. Indeed, both BMW and Mercedes have plenty

room to boast. They ended 1997 in dead heat for preeminence among luxury import brands, with BMW's sales, 122,500 vehicles edging out Mercedes' 122,417. And in a luxury-car market that grew just 6% from 1991 to 1997, BMW sales soared 130%, while Mercedes' rose 83%. That has allowed the German brands to leapfrog past their two Japanese rivals, Lexus and Acura. **BACKLASH.** What's more, if BMW and Mercedes keep accelerating, they could roar past the faltering U.S. market leaders, General Motors' Cadillac Div. and Ford's Lincoln unit, within the next few years. "Cadillac and Lincoln are definitely on the defensive," says Susan Jacobson, an independent auto analyst in Rutherford, N.J. Lincoln's car sales slipped last year, to 139,540. Even with an all-new entry-level car, the Catera, Cadillac's sales rose just 7%, to 182,624. Lincoln is bringing out a small luxury car this fall, and Cadillac is banking on a redesigned DeVille in 1999. But few expect those additions to be strong enough to slow the Germans' momentum.

Competitors now hold Mercedes and BMW up as the standard to beat. "They have clearly reframed the luxury market," says John F. Smith, general manager of GM's Cadillac Div. "I think they've been much more responsive to a variety of consumer tastes." That's just the opposite of the reputations BMW and Mercedes carried at their low point in 1991. Back then, the pair admittedly lost touch with consumers. They paid the price: Sales bottomed out at 53,433 vehicles for BMW and 58,869 for Mercedes.



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cedes—down 45% and 41%, respectively, from their high five years earlier. “The key issue then was to survive,” says Michael Jackson, president of Mercedes-Benz of North America.

BMW suffered, in part, from a backlash against its yuppie image of the 1980s, when “Beemers” were the car of choice for nouveau-riche stockbrokers and in-



BMW 328i

vestment bankers. They were known for performance, style, and such expensive maintenance that the brand's nickname was Break My Wallet. “The quality was always good, but maintenance was a huge issue,” says Steve Thomas, a BMW dealer in Camarillo, Calif. “You’d spend \$40,000 for the car, and a couple of thousand dollars a year to keep it on the road.” Mercedes, on the other hand, was known as safe, reliable, exceptionally well-engineered—and dull.

In other words, both companies were ripe for the picking. That’s exactly what the Japanese auto makers set out to do, starting with Honda’s Acura brand in 1986 and followed by Toyota with Lexus and Nissan with Infiniti in 1989. The Japanese luxury models had fresh styling, topped the quality charts, and were priced significantly lower than the competing BMW and Mercedes cars.

The way consumers flocked to the upstarts humbled the Germans. “We thought we couldn’t be touched by them, that we were superior,” says British-born Doolan, who joined BMW 20 years ago and has headed its U.S. sales operations since 1993. “There was a degree of complacency, maybe even arrogance.” The attack came as the dollar was falling against the German mark, pushing up prices of BMW and Mercedes models. When Toyota introduced its LS 400 for \$35,000 in 1989, the cheapest BMW 7-series sedan cost \$55,000, and a Mercedes 300SE sold for \$56,000. “Certainly, the Japanese did their homework, and we were vulnerable,” says Jackson, a former Mercedes dealer who became president last year. “We had to change.”

Their problems were all too apparent: bloated prices, antiquated dealer networks, and, most important, a lack of hot new cars. Both slashed prices across the board on existing products and held down costs on new models by opening

their first assembly plants in the U.S. They pressured dealers to catch up to Lexus’ standards for sales and service. BMW started a program that covered routine maintenance for a three-year period, for example.

The toughest challenge was to energize the tired lineups. Mercedes brought out two new C-class midsize sedans in 1994 and followed up with redesigned E-class full-size sedans and wagons two years later. Both new models were sportier, without a matching price hike. Mercedes ventured further into new

As German Luxury Cars Race Ahead...

U.S. SALES GROWTH, 1991-1997

BMW	+130%
MERCEDES-BENZ	+83
VOLVO	+34
LEXUS	+28
CADILLAC	-14
LINCOLN	-22
ACURA	-26
BUICK	-48
OLDSMOBILE	-61
OVERALL	+6

...Their Market Share Nearly Doubles

U.S. LUXURY-CAR MARKET SHARE

	1991	1997
CADILLAC	19%	15%
LINCOLN	16	11
BMW	5	10
MERCEDES	5	9
ACURA	12	9
LEXUS	6	7
VOLVO	6	7
BUICK	12	6
OLDSMOBILE	6	2
OTHER	13	24

DATA: WARD'S AUTOMOTIVE REPORTS

territory last year with the SLK two-seat roadster and the CLK luxury coupe.

An even bigger gamble came with the introduction last year of Mercedes’ first-ever sport-utility vehicle, the M-class, built at the company’s new factory outside Tuscaloosa, Ala. It has been a runaway hit, with 21,000 vehicles sold in the first six months. Sometime later this year, Mercedes execs will decide whether to stretch their brand even further, to cover a uniquely

American product—a luxury minivan.

BMW has matched Mercedes’ product for product. It radically redesigned its 3-series sedans in 1991 and made them more affordable to younger buyers. Currently, it offers seven versions of 3-series models, ranging in base price from \$21,960 to \$42,070. Another update for this fall has already received rave reviews from the automotive press. BMW also rolled the first Z3 roadsters out of its new Spartanburg (S.C.) factory in 1996. And next year, BMW will introduce a “sports-activity-vehicle,” described as a hybrid of an SUV and a performance sedan.

CACHET. Even as the Germans improved, they got a big break from an unexpected corner: Toyota and the other Japanese carmakers seemed to forget what had put them on the map in the first place. Lexus, for example, hit the market initially with less-expensive cars that mimicked Mercedes styling. But as Mercedes and BMW got nimble and held down prices, Lexus and other Japanese brands hiked prices to boost profits and promptly lost their edge. They have since tightened their belts by freezing and, in some cases, cutting prices.

But those moves have come too late to prevent BMW and Mercedes from capturing the hearts of many luxury buyers with their new lineups. Dr. Busse, an engineer from Port Hueneme, Calif., recently traded in an Acura for a BMW Z3. “The Z3 is more sporty, more fun,” says Busse. “BMW also has more cachet than a Japanese brand, like Lincoln or Cadillac.”

That’s a message the German paid



MERCEDES-BENZ ML 430 SPORTS VEHICLE

also trying to hammer home in their advertising. In a new Mercedes ad campaign featuring its SUVs, for example, actors dressed as executives and engineers sing and dance to a 1950s-era crooner. “I love my Benz now,” croons an Elvis-like exec. The one-word tagline is “Fun.” So far, the message seems to be resonating with Mercedes buyers. It’s the most reliable car on the road, but the image is hipper than before,” says Mary Adams, a TV newswoman from Morriston, N.J., and owner of a C-class sedan.

Of course, the German competitors are not doing everything in lockstep.

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their rivalry has intensified, executives of both Mercedes and BMW have begun to snipe at the other's accomplishments. Before a speech in Detroit in January, Jürgen E. Schrempp, chairman of Mercedes' parent Daimler Benz, suggested that BMW may have manipulated its 1997 U.S. sales figures to beat Mercedes' numbers. "They reported their sales after us, right?" Schrempp said with a smile. "The point is, if we say our sales were 122,780, they would say they had 122,781." Retorts Doolan: "If it's a sales race, let's make it a level playing field. If we include [BMW-owned] Land Rover trucks, we beat them 144,000 to 122,000."

And even as the Germans enjoy their resurgence, rivals are hardly giving up. GM's Cadillac unit is entering the luxury sport-utility fray with the Escalade, due

out this fall. Lincoln will court baby boomers—and potential C-class and 3-series buyers—with its own midsize luxury cars, the LS6 and LS8. The so-called Baby Lincolns come out this fall, with expected price tags around \$30,000.

So far, the Japanese brands have yet to mount an effective response. Lexus is bringing out a carlike SUV called the RX300, aimed directly at the M-class. In a market that's largely product driven, however, more will be needed. "The Japanese counterpunch hasn't occurred yet," says John Casesa, an auto analyst with Schroder & Co. in New York.

With the market expected to slow, however, virtually all the luxury brands are holding the line on price hikes. That means competition is likely to get a lot tougher. But the German duo is expect-

ed to continue to grab new buyers. "BMW and Mercedes are riding the wave right now," says Lincoln Merrihew, analyst with J.D. Power & Associates in Agoura Hills, Calif.

Mercedes and BMW executives voice that complacency will never creep in their companies again. Still, the surge in sales will level off, says Dietrich Zetsche, a managing director of Daimler Benz. "You will not see continued 30% growth rates," he says. Helmut Panke, a BMW managing director, agrees. "When you get to the top of Mt. Everest, you have to take a deep breath," he says. For two companies that have been to the brink, it's remarkable enough that they're on top, looking down.

By Bill Vlasic in Detroit

THE RACE MOVES TO THE CHAMPAGNE CIRCUIT

With BMW's apparent winning bid for Rolls-Royce Motor Cars Ltd. in late March, the long-simmering rivalry between BMW and Mercedes-Benz grew even fiercer. The booming German auto makers are now poised to roar into the ultraluxury end of the market. This time, the battle is about more than just sales: It's also over image and pride. Each wishes to claim it is the world's most prestigious carmaker.

Munich-based BMW agreed to pay \$570 million for the fabled British luxury marque, beating out Volkswagen and others. VW may appeal directly to shareholders of Vickers PLC, which has owned Rolls for 17 years. But BMW, which supplies 30% of the parts for Rolls's new models, is likely to prevail. If BMW's deal sticks, the investment—roughly the cost of developing a top-end luxury-car line from scratch—will give it a strong head start in a segment where prices start at \$220,000. Mercedes will have to hustle to catch up. It is close to approving production of a super-luxury car, the Maybach, but the model is at least three years from the market.

Still, the acquisition is hardly risk-free for BMW. To make it pay off, the carmaker must rev up performance at Rolls, which only recently became



CELESTIAL COSTS: Rolls's \$255,000 Silver Seraph

profitable again after years in the red. But efforts to make Rolls more efficient could damage the brand's British, burled-wood-and-leather image. Bernd Pischetsrieder, BMW's chairman, says he plans to gingerly steer his new acquisition. Production of Rolls cars will remain in the English Midlands town of Crewe. And Pischetsrieder agreed to allow Rolls-Royce PLC, the jet-engine manufacturer that still controls the Rolls name, to name one outside director.

BMW will also have to tread carefully so it doesn't undermine Rolls's high-end appeal as it invests up to \$1.7 billion over the next decade to broaden Rolls's lineup. The just-introduced, \$255,000 Silver Seraph will be joined by smaller Rolls and Bentley models that could start around \$110,000. The new models could

share engines and other major components with cars such as BMW's 5-series, holding down Rolls's costs. Exterior styling and handcrafted interiors, though, would retain their Rolls character.

The Rolls deal highlights how differently the two German carmakers have broadened their offerings. BMW's strategy has been to purchase existing companies where possible. It nabbed Britain's Rover Group Holdings PLC, with its Range Rover sport-utility vehicles,

in 1994 for \$1.2 billion. The approach has allowed BMW to enter new segments more quickly than Stuttgart-based Mercedes, which has preferred to develop new products in-house.

It's not yet clear which tactic will prove more profitable. BMW has had difficulty digesting Rover, which company officials admit may not move into the black by 2000 as planned, in part because of a strong British pound. Rolls could hit similar potholes. The company, which earned \$45 million on sales of \$500 million in 1997, currently builds only about 1,800 cars a year. That volume can plunge by half during weak economic times. And if BMW misfires with new models, Mercedes will be poised to take advantage of its old adversary.

By David Woodruff in Munich



UNLIMITED PARTNERSHIP

MIKE ROBERGE FROM ARAMARK with RALPH SCURFIELD FROM SUNSHINE VILLAGE IN BANFF, ALBERTA, CANADA

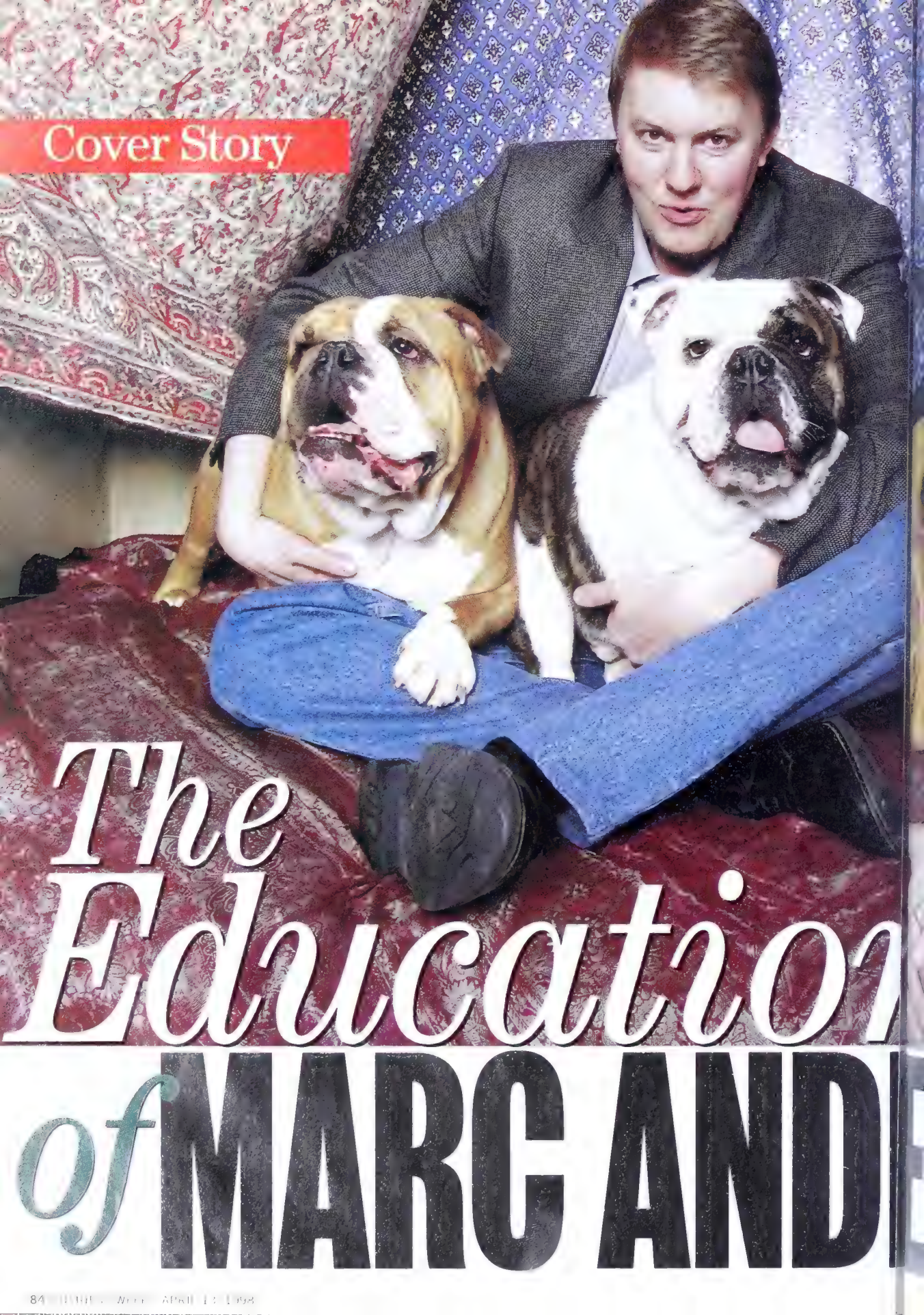
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A man with short brown hair, wearing a grey blazer over a light blue shirt and blue jeans, is sitting on a patterned sofa. He is looking directly at the camera with a slight smile. Two bulldogs are sitting in front of him. The bulldog on the left is tan and white, looking towards the camera. The bulldog on the right is white with black patches, looking towards the camera with its tongue out. The sofa has a red and white patterned cushion on the left and a blue and white patterned cushion on the right. The man's legs are crossed at the ankles.

Cover Story

The Education *of* **MARC ANDIE**

His young life has already been a roller-coaster ride. Now, it's about to get really interesting

BY STEVE HAMM

It was like a slow-motion train wreck. Marc Andreessen, 26-year-old co-founder of Netscape Communications Corp., was basking in last December's post-holiday glow when troubling reports began trickling in from Netscape's sales force. Instead of the big numbers he had hoped for, each report was more discouraging than the last. Corporate customers just weren't buying Netscape software fast enough.

By late January, the full extent of the damage was clear. Because of a huge fourth-quarter revenue shortfall, the company that had nearly turned the computing world upside down would report an \$88 million loss and fire 400 of its 3,200 employees. The news was so bad that analysts began to question the Mountain View (Calif.) company's ability to survive.

What had happened to Marc Andreessen's charmed life? It was only four years ago that this big, apple-cheeked programming whiz kid left college in the Midwest and arrived in California seeking fame and fortune. With their Web browser, Andreessen and his Netscape cohorts launched the Internet gold rush. And, thanks to the company's initial public offering, his net worth soared to \$171 million. At just 24, he appeared—barefoot and wearing a crown—on the cover of *Time*. Hyped as the next Bill Gates, he became a model for every brainy kid who dreamed of striking it rich on the Net. "He's the icon for his 20s generation—just as Gates is for his generation," says Eric Schmidt, CEO of Novell Inc.

But Andreessen has a problem. Gates has already chosen the next Bill Gates, and it's... Bill Gates. Not content just to be king of the PC realm, Gates set out two years ago to rule the Internet, too. Indeed, his move to give away much of Microsoft Corp.'s Internet

software is working so well that it threatens to level Netscape. Nor has a convincing counterattack been mounted by Netscape. "I give them an A for putting together a solid technology strategy," says Dan Lynch, an investor in Net startups. "But unfortunately you need an A+. I don't think they appreciated the lengths to which Microsoft would go to crush them."

Now, Andreessen is in the fight of his young life. No longer the hot new programming *wunderkind*, he has been forced to grow up fast. During his brief tenure in Silicon Valley, he has learned just how quickly fortunes can change in his cut-throat industry. Now, he needs to prove himself all over again—and the company's fate rests in part on his ability to remake himself as a more mature, market-savvy manager.

Through most of Netscape's early days, Andreessen occupied the relatively insulated and cushy post of chief technology officer. But as its troubles mounted, Andreessen was promoted last July to executive vice-president in charge of Netscape's 1,000-person product-development group. The move gives him a crucial role in the company's battle for survival. Today, he's in charge of making the hard product choices required for

HOMEODIES

Andreessen and fiancée Elizabeth Horn dote on Claiborne and Milo

ESSEN

Netscape to regain momentum. "Marc is extremely important to the success of the company," says Netscape CEO James L. Barksdale. "He has assumed a much bigger role, and we're depending on him to get the products out."

It's a big job, and it falls to Andreessen after an awkward and troubling period. A year ago, as the company's CTO and resident visionary, he felt sidelined by his absence of direct management responsibilities. Although deadlines were slipping and quality problems had crept into new products, Andreessen says he lacked the authority to get his ideas for change across to managers. At one point, he was so discouraged he could barely drag himself out of bed before noon.

But Barksdale was convinced Netscape still needed Andreessen's technical vision—and he took a chance by moving him into a post that would again make Andreessen central to the company. Whether the move will help fix Netscape remains to be seen. But Andreessen has rallied: He insists he's more committed than

ever to saving Netscape from the maw of Microsoft. "I know what I'm doing now has a purpose and will have results," he says. "I'm in a role to do that. I wasn't before."

The shift comes at a time of stiff challenges for the adolescent company. Though revenues have raced to \$534 million in the past 2½ years, Netscape's share of the browser market has dwindled from 80% to about 60%. Meanwhile, Microsoft's share has zoomed from 5% to 40%. Netscape lags in the corporate E-mail business, and it faces fierce competition



from giants such as Microsoft and IBM in key markets such as software for Web sites and E-commerce. It's no wonder that many analysts say Netscape would be better off selling out to a bigger player—such as Sun Microsystems Inc. or IBM.

Does Andreessen have the fire-in-the-belly commitment of a Michael Dell or the survival instincts of an Andy Grove? Perhaps, but he seems to be hedging his bets. He says that if Netscape were sold, it wouldn't be so bad—if the buyer were a company that shares its goals. And in February,

Cover Story

MARC ANDREESSEN'S INTERNET

SEPTEMBER, 1989

Leaves home to attend undergraduate school at the University of Illinois at Urbana-Champaign.

JANUARY, 1992

Begins a \$6-an-hour software programming job at the National Center for Supercomputing Applications.

NOVEMBER, 1992

Starts working on a World Wide Web browser, Mosaic, with co-worker Eric Bina. The



numbers of consumers for the first time.

APRIL, 1993

NCSA releases Mosaic to the public. In December, Andreessen graduates from the University of Illinois with a BS in computer science.

JANUARY, 1994

Arrives in Silicon Valley to work for a Net startup, Enterprise Integration Technologies.

APRIL, 1994

Leaves to start Netscape with Jim

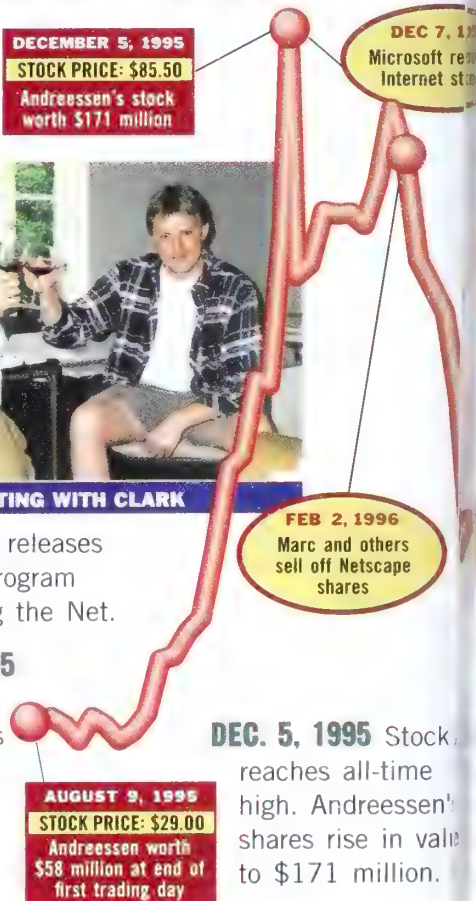


TOASTING WITH CLARK

Clark. Soon releases Navigator program for browsing the Net.

AUG. 9, 1995

Netscape IPO*. Shares soar from \$7 to \$36 before closing at \$29.



reaches all-time high. Andreessen's shares rise in value to \$171 million.

software program paves the way for opening the Internet to huge





“I saw the stock price and went, ‘Eek!’ We thought the IPO would be successful. But we didn’t dream it would be that successful”

THE 1995 IPO BASH: ANDREESSEN IS SECOND FROM THE LEFT, CLARK IS AT THE FAR RIGHT

aded 375,000 shares—or about 25% of his Netscape hold—when the stock price was near an all-time low. Anssen claims he’s not bailing out, just diversifying his ings. But, says Bob Gabele, an analyst at insider-trading er CDA/Investnet, Andreessen is sending exactly the ig message to investors: “It’s not a good sign.” Perhaps Andreessen is just being realistic. After all, he vs that a Netscape takeover or fluctuations in its stock e are beyond his control. So he ignores such issues—im-

mersing himself in the job at hand. This blinder-style focus also helped him through the dark days of January. “The first thing you do is say: ‘Oh, s—!’” he admits. But he has long since sized up the situation rationally like the engineer he is at heart: “You think about what we need to do. It’s a fork in the decision tree. It’s a matter of figuring out what all the options are and what’s the right path to take.”

Two years ago, it looked as if Netscape’s path would always lead upward. So it would be understandable if Andreessen were emotionally devastated. He says he’s not. He swears he never believed the hype that surrounded Netscape. “What happened to me happened so quickly and was so far out of proportion to anything that would be considered reasonable that I treat it as an external phenomenon,” he says in his rapid-fire delivery. He was happy to be a high-profile evangelist for the Internet—as long as it helped boost Netscape’s fortunes.

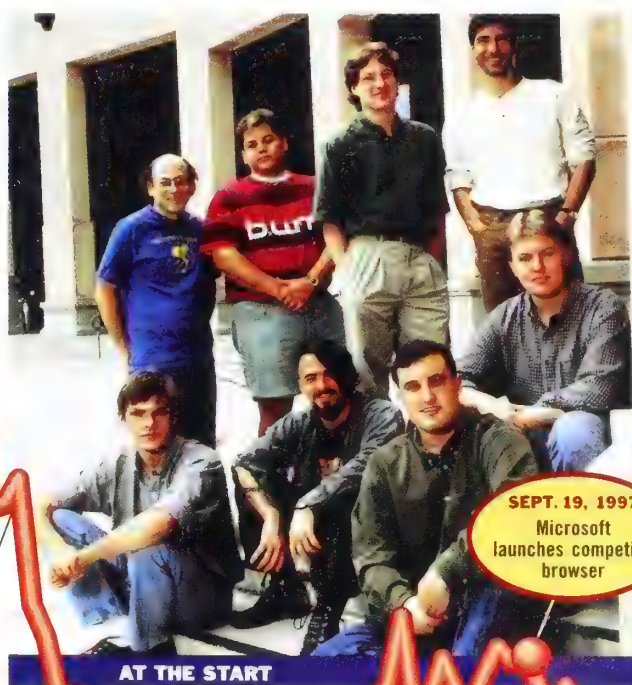
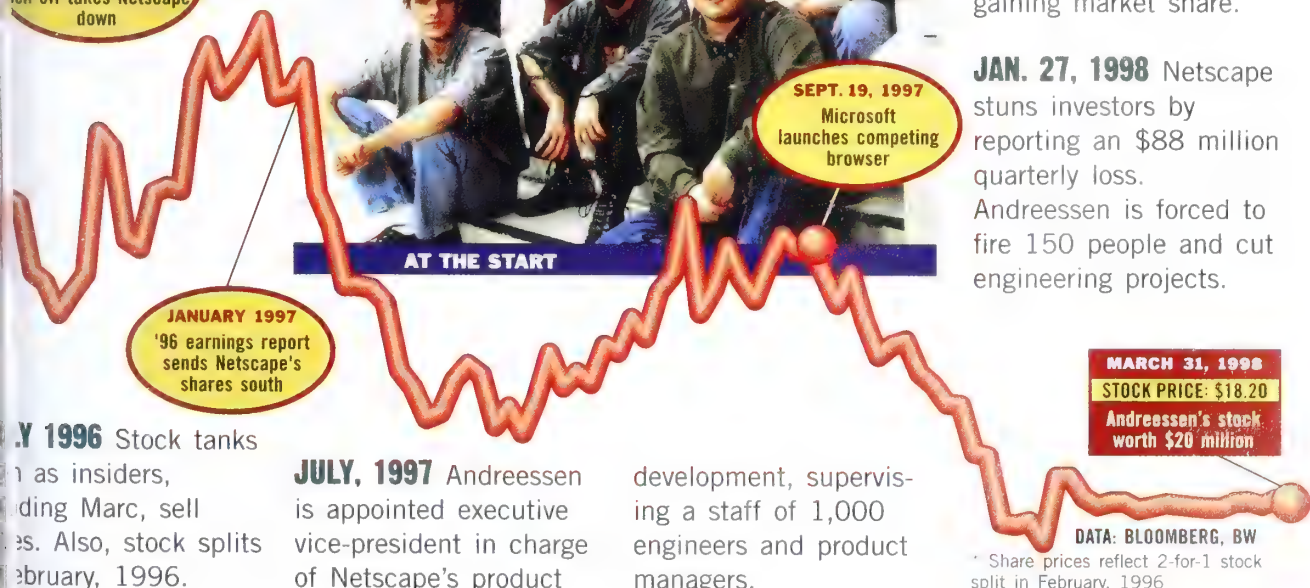
FASTER TREADMILL. But Andreessen couldn’t have guessed his glory days would be so brief. Indeed, he has had to grow up in Internet Time, a term first used to describe how quickly Netscape delivered new products (originally every six months, a breakneck pace). Bill Gates got to run Microsoft for more than a dozen years before IBM set its sights on him. For Netscape and Andreessen, the trip from phenom to potential has been over in a blink of an eye.

That phenom was the Marc Andreessen everyone thought they knew—the hamburger-chomping pop icon for the cyber generation. But just beneath the surface, there’s a much more complex person—not so happy-go-lucky, not so easily typecast. More than anything, Andreessen is restless, impa-

YSSEY

JULY 7, 1995 Microsoft’sounced plans to focus strategy on the Internet sends investorsng.

MAY-DEC. 1996
industrywide
sell-off takes Netscape
down



THESE ENGINEERS (ANDREESSEN, RIGHT) HELPED FOUND NETSCAPE, WHOSE BROWSER EVOLVED FROM ONE THE GROUP HAD WORKED ON AT THE UNIVERSITY OF ILLINOIS

SEPTEMBER, 1997

Microsoft launches its Internet Explorer 4.0 to rave reviews. Analysts report that the giant is gaining market share.

JAN. 27, 1998 Netscape stuns investors by reporting an \$88 million quarterly loss. Andreessen is forced to fire 150 people and cut engineering projects.

JANUARY 1996 Stock tanks as insiders, including Marc, sell shares. Also, stock splits in February, 1996.

Cover Story

tiently jumping from one ambitious undertaking to the next.

Shortly after launching Netscape, he gave up software programming, a passion of his for years. He has become a fan of classical music—after working his way up the ladder through rock and jazz. Before, he was content being Netscape's CTO. Now, management is his focus. "Once he finishes with something, he just leaves it behind, like an old gym bag under your desk," says Netscape co-founder Eric Bina.

Andreessen doesn't exactly see it that way. For him, it's all about acquiring as much knowledge as he can as fast as he can in pursuit of the next Big Idea. But his first big idea will

BIG IDEAS?

Barksdale and Andreessen meet weekly to brainstorm



be hard to beat. As a student researcher at the University of Illinois at Urbana-Champaign, he took the lead in creating the first popular Internet browser, called NCSA Mosaic. Then, at Netscape, he conceived a new browser that added features normally found on operating systems such as Microsoft's Windows. From there, Andreessen was one of the first to envision intranets—communications networks that promise to turn companies into information dynamos.

In its race to create Internet services that can compete with Microsoft, Netscape is relying on Andreessen's fertile mind to come up with hot new products. Is he up to the challenge? There's no question he has grown tremendously in the past two years, often by absorbing painful lessons. Barksdale, for instance, once locked Andreessen out of a morning staff meeting when the night-owl youth had arrived late one time too many. It was meant as a joke, but it got Andreessen's attention. Now, Andreessen is one of the most punctual people on Barksdale's staff. "He's come a long way," says Barksdale.

Andreessen has acquired more grown-up tastes, too. The



DON'T OVERDO
Andreessen discourages colleagues from working over hours a week

chubby 6-foot, 4-inch lad who dressed in shorts, T-shirts and sandals in 1994 has shed about 30 pounds and now favors Ermenegildo Zegna suits and Robert Talbot shirts. Greasy hamburgers and milkshakes are out, replaced by grilled salmon and chardonnay. And he has traded in his red Mustang for a more sober white Mercedes-Benz S600 sedan.

It's one thing to learn to dress well and show up on time and quite another to help save a troubled company. Some servers question whether Andreessen has the managerial skills needed for the job. After all, before his promotion last summer, he had never managed more than a handful of people. "In the Internet market, things are changing so fast," says the CEO of another Internet software company. "My youth and inexperience are hard to overcome."

SHOWTIME. Others say it's time for the sometimes-cocky Andreessen to deliver the goods. "The challenge for Netscape is to live up to the story they've been telling everyone—they were going to be the next Microsoft, they were going to put us out of business and become the next platform for the industry," says Nathan P. Myhrvold, CTO at Microsoft.

Andreessen never claimed he would put Microsoft out of business—but he boasted often in Netscape's early days that the Web would make operating systems such as Windows irrelevant. Now, it is clear just how wrong he was. Since Microsoft's launch of Windows 98 and its integrated Web browser just two months away, Andreessen needs to put his self-improvement campaign to the test.

As the head of product development, he has a key role in implementing Barksdale's strategy of trying to get Netscape back on the profit track by shifting its focus away from

ser market. Instead, the pair to concentrate on sophisticated rare for running large corporate orks. Andreessen will also have accelerate the rollout of a suite of mmerce applications. And he is ing resources into its new Net- r Web site—hoping to turn what ready the top business site into o. 1 site for consumers as well. ill, Netscape hasn't given up- y on browsers. Andreessen pioned the idea of offering its ser source code to all comers.

a novel concept: By essentially sharing cape's intellectual property with the world, eessen is betting the company will be flood- ith new—and free—ideas from outside soft- developers. The best would then be includ- i communications software packages for op PCs that Netscape will sell to corporate mers. The next several months will demon- e whether the move succeeds. "If we don't his off," says Andreessen, "it will be our own fault."

FORM. To help Andreessen hone his skills, Barksdale aken him under his wing. The two meet almost every day for a working lunch where Andreessen usually s a long list of ideas and issues. "The best lesson I ed from Jim is to apply a balance between urgency and nce," says Andreessen. "You set up a flow to people's so they're not always racing. Give them enough res- es to do their jobs. Give them consistent direction."

ll, nothing could have prepared Andreessen for the ching decisions he has had to make in the past two is to realign Netscape's engineering organization. Hardest was cutting 20% of his expenses—and 150 people. "The thing you can do is try to gloss things over," he says, ex- ng how he broke the news to employees. So, he met with the entire engineering group in January eld two to three "brown bag" lunches a week ll comers. The face time has helped boost e. "He's steering the ship through a storm," dreessen has remained close to the rank- le programmers since Netscape's early days. y, it's because he's a techie at heart. But it's ecause he enjoys hanging out with people his age. Case in point: his movie nights with



WATCHFUL EYE

John Doerr says Andreessen "has grown a lot, and it's not over"

pals. On a recent Friday, Andreessen and a half-dozen others, mostly from Netscape, sat in the second row at the Century Cinema in Mountain View and hooted at the plot twists in *Palmetto*.

If that sounds like a bunch of kids, it should. Having a laugh is still very high on Andreessen's "to do" list. How else could he handle the pressure of competing with mighty Microsoft every day? To lighten the stress on the job, he still resorts to self-mocking humor, like the time he came to a meeting wearing a Spandex outfit and roller blades after losing a bet with engineers that they wouldn't get a product out on time. And in stark contrast to Microsoft's legendary workaholic culture, Andreessen encourages his workers to limit office time to 50 hours a week.

Andreessen insists that obsessing over Microsoft's advancing guns does no good. So he makes the most of his own free time at the

Mediterranean-style house he bought three years ago in Palo Alto. He lives there with his fiancée, Elizabeth Horn, a freelance Web-site designer. Horn has decorated the place with Turkish rugs, potted palms, a sizable collection of Buddhas, and a stunning, five-foot-tall Moroccan wedding couch made of white brass that serves as a daybed for the couple's three gravel-throated English bulldogs—Claiborne, Lily, and Milo.

If Andreessen's work life has become more structured, at home, it's still fun and games. A couple of weeks ago, on a lark, Horn dyed Milo teal—one of Netscape's logo colors. And the pair kick back by popping into their 36-inch Mitsubishi TV such B-movies as the John Woo shoot-'em-ups *The Killer* and *Hard Boiled*. Other evenings are spent engrossed in his-and-her Web surfing at side-by-side computers.

What they don't do much is go out on the town. That's because Andreessen is notoriously private and shy around strangers. On a recent Saturday, while Horn sat in their breakfast nook talking about their relationship, Andreessen pattered nervously nearby—cringing. "I have a huge amount of trouble with these personal questions," he said later. "It's a Midwestern thing."

Andreessen is from the very heart of the Midwest—New Lisbon, Wis., a village of 1,500 in corn-and-dairy country. He grew up 10 miles out-

COACHES

Barksdale and Clark have helped hone his management skills



Learning from early mistakes, Andreessen is throwing most of Netscape's engineering talent into just a few products

side town on Castle Rock Lake. His mother, Pat, works in customer service at Lands' End. His father, Lowell, now retired, was a sales manager for Pioneer Hi-Bred International Inc. Andreessen has a jaundiced view of his dad's job: "It was an Amway kind of thing—farmers slowly going out of business on their family farms sell seed corn to other farmers slowly going out of business."

Don't ask Andreessen to talk more about his family—he clams up. The subject is so sensitive that he first declined to provide even the names of his parents or his brother, Jeff, a history major at the University of Wisconsin. Since leaving the Midwest in 1994, Andreessen has had little contact with his family. His brother insists "there is no animosity between any of us." Still, he is troubled. "The last time I spoke to him was four years ago when he went off to California," says Jeff. "There's resentment. I'd like to hear from him."

Jeff describes their childhood as a happy one. Marc discovered programming at age 12; recuperating from an operation, he persuaded his parents to buy him a Radio Shack computer.

Soon programming became his passion. "It's a way to be creative and express ideas in a way you can touch," he says. It also helped relieve the boredom of growing up in the sticks. "He made it clear he was going to get out of town when he graduated," recalls childhood friend Richard Hoile.

First, Andreessen established himself as a top student at tiny New Lisbon High School (student population: 240). He annoyed some teachers by questioning the relevance of their assignments. Once, an English teacher asked for a collage on the topic of love, and Andreessen objected that it was too childish. "Some people thought he was cocky. I thought he was just self-assured," says social studies teacher Eugene Gibson.

At the University of Illinois, Andreessen got a programming job at the National Center for Supercomputing Applications, a university-affiliated research center. Earning \$6 an hour, he learned about the Web and with colleague Bina created a prototype for the Mosaic browser. Others elsewhere were working on browsers, too, but according to Tim Berners-Lee, director of the World Wide Web Consortium and the creator of the Web, Andreessen understood how to appeal to consumers. "He made it simple to install and use," says Berners-Lee.

It wasn't long before Silicon Valley beckoned, and Andreessen headed West. He landed at Enterprise Integration Technologies (EIT) with a salary of \$80,000—unheard of for a starting programmer. He often coded alone at night as he listened to opera at full blast and downed Pepperidge Farm Goldfish. "He reminded me a lot of [Apple Computer Inc. co-founder] Steve Jobs," recalls Marty Tenenbaum, who ran EIT and now is chairman of the CN Group, an E-commerce startup. "He was intense, driven, and focused."

One day, a little over a month into his West Coast adven-

ture, Andreessen got an E-mail message from James Clark, the founder of Silicon Graphics Inc., who knew about Andreessen's role in creating Mosaic and wanted to talk to him about going into business together. In a series of brainstorming meetings, they noodled over a concept for a Nintendo online game service—but dropped it. Other ideas came and went. Then, at about 1 a.m. on Mar. 25, 1994, after a leisurely dinner and several bottles of burgundy, Clark left up to Andreessen to decide what they should pursue. There was a pregnant pause. "We could always create a Mosaic killer—just build a better product and build a business around it," Clark remembers Andreessen saying.

WHITE PAPERS. To pull that off, Andreessen and Clark moved fast to round up the core engineering crew at NCSA—and then raced to produce a commercial browser before anybody else could. During his first six months at Netscape, Andreessen played the role of unofficial product manager, but once Netscape Navigator was launched in December, 1994, Andreessen became full-time visionary and evangelist—winning the title of CTO.

The job suited him fine. He paid to think about how Netscape could turn the Web from a chaotic experiment into an exciting medium for consumers and a powerful communications tool for corporations. He wrote long white papers chock-full of strategic technology plans. At conferences and PR events, he spread the word about the Web and Netscape.

The payoff came on Aug. 1995, with Netscape's IPO. Andreessen woke up late, as usual. He logged on to his computer. Netscape's stock had been priced at \$14 but hit \$75 before closing at \$58. "I saw the stock price go up, went, 'Eek!'" says Andreessen, who owned 1 million shares before a 2-for-1 stock split six months earlier. "We thought the IPO would

be successful. But we didn't dream it would be that successful."

Then, gradually, Andreessen's work became stale. In the early days, being Netscape's CTO was a crucial role. Andreessen charted the company's long-term technology direction. And engineering managers listened to his ideas because he was a founder. As Netscape grew up, however, the focus was more on getting products out the door and into the hands of corporate customers, and Andreessen was troubled that his job was less vital.

By last spring, the Internet guru had fallen into a slump. Tired on the road, Andreessen felt out of touch with many of the key product decisions. With no management responsibilities of his own—the two top engineers reported directly to Barksdale—Andreessen was "on a trajectory to become a surehead," says Eric Hahn, a former engineering manager who is now Netscape's CTO. He spent his days meeting with customers, giving interviews, and making speeches on the wide world of the Internet while having less and less to do with solving the problems Netscape was facing. Admits Andreessen, "I wasn't doing much, and there wasn't much for me to do."

Indeed, it was no longer clear what he was supposed to

NETSCAPE'S SURVIVAL STRATEGY

To reverse its sagging fortunes, Netscape must act fast to:

- Develop and quickly get to market new and better browsers, Web servers, and corporate intranet software
- Persuade corporate customers to pay a premium over Microsoft's basic software giveaways
- Build up its software to fully exploit the booming E-commerce market
- Turn its Netcenter site into a popular consumer Internet gateway to rival America Online and Yahoo!

Cover Story

headed West. He landed at Enterprise Integration Technologies (EIT) with a salary of \$80,000—unheard of for a starting programmer. He often coded alone at night as he listened to opera at full blast and downed Pepperidge Farm Goldfish. "He reminded me a lot of [Apple Computer Inc. co-founder] Steve Jobs," recalls Marty Tenenbaum, who ran EIT and now is chairman of the CN Group, an E-commerce startup. "He was intense, driven, and focused."

One day, a little over a month into his West Coast adven-

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doing. "Part of it was, my personality had changed. I had more ideas about how we should be running the company, but I wasn't in a position to change things," he says.

Meanwhile, to others, Andreessen seemed distracted and adrift. "Many of the newer employees had never met him, much less interacted with him," recalls Hahn. Quincy Smith, Netscape investor relations director and a friend, says Andreessen was obviously disturbed. "He was frustrated. Outside of work, he didn't talk

Cover Story

about Netscape as much," recalls Smith. Andreessen remembers it like this: "More and more of my days I was shifting into a pattern of sleeping until noon or later and rolling in to work at 2 and heading for home at 6."

Barksdale noticed, too—but even as Andreessen floundered, he continued to believe deeply in him and his abilities. So Barksdale fixed on a strategy aimed at recharging Andreessen by giving him a more important job while simultaneously addressing nagging problems in engineering.

Netscape was losing its technology lead over Microsoft, particularly in browsers. And the company's two top engineers were in transition—one, Hahn, was going on sabbatical, and the other, Rick Schell, had asked for a less intense job. So Barksdale created a single engineering group and put Andreessen in charge of it—backing him up with a cadre of seasoned engineering managers.

Is Barksdale's strategy a stroke of genius or an act of desperation? He insists no one at Netscape has better technical know-how than Andreessen. And he is convinced that, with guidance, Andreessen will succeed as a manager.

"Marc was frustrated with the problems in engineering, so I said if he's so frustrated, why not let him do it," says Barksdale.

Andreessen knows he still has a lot to learn. And that often means looking back at the mistakes Netscape has made. It tried to do too many things at once—assuming it would succeed at everything. Andreessen now practices the art of the possible. He's putting most of Netscape's engineering resources into a handful of major products. Andreessen and his colleagues also failed to spot the potential for turning the Netscape Web site into a marketplace of content and services to rival the popularity of Yahoo! Inc. and America Online Inc. It wasn't until last October that they launched Netcenter, their content-oriented Web site. "Our biggest mistake was we didn't think of this two years ago," admits Andreessen.

Will the latest strategy be enough to stave off Microsoft and save Netscape? It's a long shot, according to analysts and industry players. Despite Netscape's risky giveaway of its source code, most predict it will lose browser market share even more quickly once Microsoft comes out with Windows 98. And in servers, Microsoft keeps upping the ante by

adding new features to basic servers it gives away with Windows NT operating system.

To stay in the race, Netscape will have to bolster its own server technology while holding prices low enough to keep corporate customers in its fold. Mary McCaffrey of BT America Inc. says she expects more bad financial news in the next couple of quarters. Longer term, there's a ray of hope. "If they knuckle down and get focused on the strength of their product line, they've got a shot at turning this around," she says.

RELENTLESSLY POSITIVE. Andreessen's transformation from smug dreamer to a realistic doer has been closely monitored by others in the industry. Patricia Sultz, general manager of Java software for IBM, has noticed that Andreessen no longer talks about Netscape going it alone. Instead, he's open to collaboration. "He's a more pragmatic businessman," she says. John Doerr, a venture capitalist with Kleiner Perkins Caufield & Byers and an Andreessen mentor, says Andreessen isn't a wild-eyed rebel anymore. "He has retained his fresh point of view about what's possible," says Doerr. "But now he listens much better. He has grown a lot, and it's not over."

Andreessen does not indulge in self-analysis—unless to press him. What does he feel about being so rich—the \$171 million peak—and then seeing his net worth drop by more than two-thirds, to about \$50 million? "Money matters," he says. "But it's not a big focus. It's not the motivator or even a measure of my success." Why is he relentlessly positive in the face of Netscape's problems? "I don't waste time being depressed," he says. "If you're not happy, you should change what you're doing." What most is proving himself all over again, becoming a good



“I know what I’m doing now has a purpose and will have results. I’m in a role to do that. I wasn’t before”

manager and learning how to build a company. "I need more raw experience," he says. "I've read and watched a lot of things, but I haven't done a lot of things."

Outsiders foresee an important role for Andreessen in the computer industry—whatever happens with Netscape. "The Internet is still a raging pagan beast. It's not yet easy. But it could make it easier," says David Siminoff, a portfolio manager at Capital Research in San Francisco. And while it's unlikely that Andreessen will change the world again with another Mosaic-like discovery, Mary Meeker, an analyst at Morgan Stanley Dean Witter & Co., says: "He'll be a great CEO—5 to 10 years from now."

For somebody as restless as Andreessen, a decade is a long time to wait to be anything. But maybe the young man who was always in a hurry is now ready to learn another valuable lesson: the virtue of patience.

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Additional stories, including an extensive interview with Marc Andreessen, can be found at www.businessweek.com.

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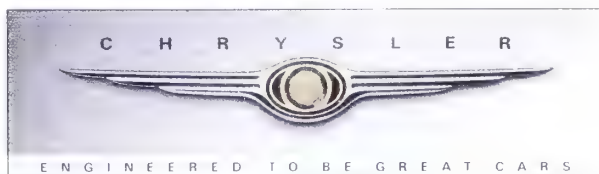
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BUYOUT FIRMS

BLACKSTONE: NICE IS FOR SUCKERS

Its good cop-bad cop team grabs the No. 2 spot in LBOs

It has been an exciting week for Stephen A. Schwarzman, chief executive of the Blackstone Group. He and real estate developers Mortimer B. Zuckerman and George Klein just won the last two development sites on New York's red-hot 42nd Street. Price: a sky-high \$330 million. And splashed all over the London press are reports that Blackstone has bid more than \$800 million for the Savoy Group, a group of London five-star hotels. "According to my competitors, I'm this young Turk with this great advantage who is unfairly buying up the world, but I can't touch Blackstone's price," says Barry S. Sternlicht, CEO of Starwood Hotels & Resorts Worldwide Inc., who also is involved in bidding for the Savoy.

When it comes to being aggressive, Schwarzman stands out even by Wall Street standards. And his aggressiveness isn't limited to bidding top dollar. His abrasive and imperious management style has earned him enmity from former partners, some of whom have left over the years. One ex-employee says Schwarzman goaded him by saying, "You're dog meat," which Schwarzman denies. Schwarzman, 51, also inspires an unusual number of derogatory comments from competitors. Among the milder ones: "He's a control freak. He thinks he's intellectually superior."

"ANCIENT HISTORY." Yet Schwarzman and Peter G. Peterson have built Blackstone into one of the most successful small investment banks around through smart hiring and good timing. They own or have major stakes in 23 companies with revenues totaling \$14 billion, including cellular provider CommNet Cellular Inc. and auto parts supplier American Axle. And Blackstone is a major investor in commercial real estate. One former partner, Henry R. Silverman, CEO of Cendant Corp., says: "In spite of interpersonal issues, we were able to make a ton of money for our investors." Says Schwarzman: "I was probably too tough on people, but that's ancient history in the firm's evolution."

Founded by Peterson and Schwarzman in 1985 with \$400,000, Blackstone has climbed to No. 2 behind the reigning buyout kings, Kohlberg Kravis Roberts & Co. In 1997, Blackstone raised \$3.8 billion for its third buyout fund—in large measure because its second one had annual returns of more than 52% through December, 1997, net of fees, says Schwarzman. "At this point in the fund's life, they've been one of our superior performing private equity funds," says H. Carl McCall, New York State comptroller. Now, Schwarzman must demonstrate that his LBO team, which includes former Budget Director David A. Stockman, can invest the billions it has raised when the LBO market has never been frothier. Indeed, in a \$1.9 billion deal in March, Blackstone was outbid for Safety-Kleen Corp., an environmental services provider.

And Schwarzman must keep his partners happy. "He and Pete suck off a disproportionately large percent of the economics," says one banker. For example, if the real estate fund makes \$100 million, investors would get \$80 million while Blackstone would get \$20 million. The 25-person real estate team, in turn, divvies up \$10 million, while 13 Blackstone partners split \$5 million, with about \$5 million going to the top two. Schwarzman says the two unequivocally control Blackstone, but insists tight control eliminates infighting while allowing employees a voice. Says Schwarzman: "A lot of places have blown up because control was not centralized."

Schwarzman knows this from bitter experience. When Lehman Brothers Inc.,

PETER G. PETERSON

*Chairman,
The Blackstone Group*

AGE: 71 **EDUCATION:** Northwestern; MBA, University of Chicago **JOBS:** Lehman Bros.; Co-founded Blackstone **PERSONAL:** Married to Joan Ganz Cooney, five children

was ripped apart in a nasty power struggle in 1983, Peterson was ousted as CEO. Schwarzman, a Lehman merger and-acquisitions banker, brokered Lehman's sale to American Express Co.'s Shearson. But right after the deal closed, he shocked Shearson top brass by saying he wanted out, leaving them with a deal that he initiated.

After some lean early years, Schwarzman and Peterson transformed themselves from deal advisers to far more lucrative dealmakers. Schwarzman's skills, joined with Peterson's gentlemanly way, extensive corporate Rolodex and credentials as a former Comptroller Secretary, helped reel in blue-chip



BLACKSTONE'S BUSINESSES

LEVERAGED BUYOUTS Raised \$3.8 billion in 1997 fund. Owns all or part of CommNet, a rural cellular provider; Clark, an oil refinery; Allied Waste; and Graham, a plastic-container maker.

REAL ESTATE Raised \$1.2 billion fund in 1997 and \$350 million fund in 1995. Owns Boston's Ritz Carlton, Chicago's IBM Building, and New York's Worldwide Plaza.

M&A Clients include Japan's Sony, Sweden's Autoliv, and American Stores. Has alliances with Japan's Nikko Securities and Sweden's Enskilda Securities.

BANKRUPTCY ADVICE Run by Arthur Newman, formerly head of Chemical Bank's bankruptcy practice. Clients include Barney's, Caldor, and Levitz Furniture.

ASSET MANAGEMENT Markets a fund-of-funds that invests in leading hedge funds. Has over \$1 billion under management.

DATA: THE BLACKSTONE GROUP



STEPHEN A. SCHWARZMAN

*President and CEO,
The Blackstone Group*

AGE: 51 **EDUCATION:** Yale, Harvard business school **JOBS:** Lehman Bros., Co-founded Blackstone **PERSONAL:** Married to attorney Christine Hearst, two children

that before Loewen can buy back all of Prime Succession in 2001, Loewen must first pay Blackstone at least a 25% annual return on the \$52 million Blackstone invested. This built-in exit strategy and pre-carve-up of returns greatly reduces Blackstone's risk, which holds great appeal to Schwarzman. "Steve is driven by insecurity, which helps them, since he is always worried about the downside," says a colleague.

Loewen's performance has been disappointing recently, but Schwarzman says it won't affect Blackstone. But the firm's most profitable buyout, UCAR, may haunt it. Blackstone owned UCAR International, a graphite-electrode maker, from 1995 to April, 1997. In late 1997, the Justice Dept. launched an industry-wide price fixing inquiry and is looking at the period when Blackstone owned UCAR. And four Blackstone directors have been named in a

such as Duracell International Inc., and hasn't done multibillion-dollar deals. Blackstone bets on reliable returns from dull, industrial companies. And it has only bought companies for less than \$1 billion. Schwarzman also thinks he deserves credit for building five lines of business (table), compared with KKR's focus on LBOs. He snipes: "KKR is a one-trick pony."

Schwarzman, whose father owned a Philadelphia dry goods store, has little reason to feel slighted. He attended Yale University, where he launched the Yale Ballet Society as a clever way to meet women, and Harvard business school. An inveterate name-dropper, when asked for a few friends' names, he supplied a two-page memo listing 20 "old friends," including dealmaker Bruce Wasserstein and Reed E. Hundt, ex-Federal Communications Commission chairman.

Schwarzman rebounded from a devastating 1991 divorce, where he had to pay his first wife, Ellen Schwarzman Katz, more than \$20 million, estimated to be half of his then-net worth. Still, *Financial World* calculated that he made \$45 million in 1996 alone. Schwarzman was remarried in 1995 to Christine Hearst, an attorney. He gets around in a helicopter he owns with Peterson, and has homes in Manhattan, East Hampton, and Jamaica.

The booming markets will provide riches enough to keep Blackstone's 250 employees happy. Schwarzman says that its LBO fund will have no trouble generating 25% to 30% annual returns without taking more risk. He says Blackstone can add staff to maintain its 1997 investing pace of \$700 million. Says Blackstone partner J. Tomilson Hill: "Pete and Steve have built an institution of permanence." If so, it would be a triumph of ego over charm.

By Leah N. Spiro in New York, with Kathleen Morris in Los Angeles

funds and corporations to the LBO

two men created a strong niche: LBOs with companies that temporarily warehouse an acquisition with Blackstone. In 1996, for example, Loewen, a Canadian funeral home consolidated, faced a cash crunch and couldn't debt to buy funeral home chain Succession Inc. The two created a vehicle to buy Prime Succession that 4% owned by Loewen and 76% by Blackstone. This let Loewen a \$300 million purchase off-balance since minority stakes don't have to solidated in its financials. complicated agreement stipulates

lawsuit by UCAR shareholders.

The outlook is rosier for real estate, which Schwarzman timed just right. In 1992, as the boom began, he hired three real estate pros who raised \$350 million and bought such properties as New York's Worldwide Plaza, which is now for sale. The fund had annual returns of 50% through 1997, says Schwarzman, and in 1997, the group raised \$1.2 billion in a second fund.

Now Schwarzman seems intent on being recognized as a major financier. His biggest rival is Henry Kravis. Schwarzman believes Blackstone is slighted in the press because, unlike KKR, it doesn't own companies with household names,

A FEVERISH BATTLE BREAKS OUT ON YOUR DESK

Reuters vs. Bridge vs. Bloomberg—and room for only two big guns

For years, the \$7.5 billion business of delivering instant financial numbers and news was ruled by two rivals: Reuters Holdings PLC, by far the worldwide leader, and Bloomberg LP, the brash, fast-growing upstart. They fought for the same users, but wound up side by side on many desks. Reuters specialized in foreign exchange and European news, while Bloomberg offered sophisticated financial analytics.

That changed on Mar. 17, when Bridge Information Systems Inc., long regarded as an also-ran, burst onto the scene by paying \$510 million for Telerate, Dow Jones & Co.'s money-losing bond-pricing arm. The acquisition could be one of those rare one-plus-one-equals-three deals. Reuters remains the leader by far, with 386,000 desktops. But Bridge, with 169,000 users, will eclipse Bloomberg, with 92,000, as the No. 2 provider. Says Ashish Shah, head of equity arbitrage at Bankers Trust New York Corp., who uses Reuters and Bloomberg: "There's warfare for your eyeballs."

Which services will users such as Shah keep? Only two major providers are likely to wind up delivering the real-time data and news that grease financial markets, as traders, financial analysts—and a growing contingent of corporate execs—cut information clutter. "Desktop real estate is more precious than ever," says Michael Wolf, the media partner at Booz, Allen & Hamilton Inc. "Most don't have room for more than two real-time data services."

The winners will split one of the hottest segments of the information economy. With record numbers of mergers and acquisitions and new brokerages investing staggering wealth, spending on financial data and news grew 9.6% in 1997, to \$7.5 billion, and will top \$10 billion by 2000, according to Veronis, Suhler & Associates. "The number of desks where you can put a terminal is ex-

ploding," says Michael Bloomberg.

Bloomberg, who has made billions feeding the demand, will have to fight harder than ever. Bridge was a \$130 million laggard until 1995, when it was purchased by Welsh, Carson, Anderson & Stowe, a powerful investment bank with a history of building businesses through acquisitions and spinning them off. It engineered a series of deals, including the 1996 purchase of Knight-Ridder News Service. Bridge will have \$1.1 billion in sales after swallowing Dow Jones Markets—to be renamed Bridge/Telerate.

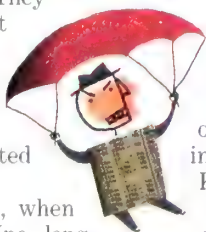
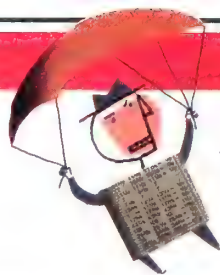
Absorbing Telerate won't be easy. Because of customer defection to more comprehensive services, Telerate lost \$70 million to \$100 million last year, say insiders. Its technology and culture differ vastly from those of Bridge, which lost some desktops after previous mergers. "We had to hold the hands of our customers," says

Patrick Welsh, a partner in the investment firm that owns half Bridge. "We gave them incentives to stick with us as we achieved something much larger."

Since buying Bridge, Welsh's firm has poured tens of millions of dollars into its database, technology, delivery systems, and management. It also tapping customers that have never used real-time data. Bridge collaborates with the New York Stock Exchange to put terminals on the desks of 6,000 chief executives and chief financial officers to get instant trading information. And Bridge is penetrating newsrooms, where Bloomberg has gained price-less publicity by swapping machines for bylines.

Bridge, though, has a serious vulnerability: The key contract that gives it leading government-bond pricing is in jeopardy. Cantor Fitzgerald LP, the biggest seller of Treasury bonds, supplies exclusive data to Telerate's 940 customers—at \$30 a head per month. When the contract shifts from Dow Jones to Bridge, Cantor wants payment for the 750 users Bridge already had. Bloomberg argues that the contract is limited to the Telerate customers, leaving the difference at \$27 million annually.

The contract, which expires in 2006, is crucial for Telerate. Virtually all bond prices are benchmarked against prices of T-bills—and Cantor



Squaring Off

What the deliverers of real-time financial data and news offer

	REUTERS	BRIDGE/TELERATE	BLOOMBERG
DESKTOPS	386,000	169,000	92,000
PRICE PER MONTH	\$800 to \$1,200	\$150 to \$750	\$1,200
DISTINCTIONS	Extensive news-gathering and foreign-currency exchange	Treasury-bond prices and a system that lets customers download data	Strong tools that let customers analyze financial and historical data

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is the biggest seller. In an internal poll last year, customers said they would dump Telerate if it weren't for the Cantor data, according to an insider. If Cantor prevails, Bridge would have to hike its current rates by \$45 a month—a 50% jump for bottom-tier customers—to turn a profit, say sources close to the deal.

That would kill its edge as the lowest-cost provider of real-time data. Right now, Bridge sells its services à la carte, providing bare-bones equities data for \$150 per desktop, and up to \$750 for its entire menu. It also offers an "open" system that lets customers download data to their own PCs and merge them with outside data and programs. "Our rallying cry is, we give our clients more choices, better price, and more open systems," Bridge CEO Thomas Wendel says.

BUZZWORD. Reuters also has an open system and charges \$800 to \$1,200, depending on the data desired. But it is threatened by the expected arrival of the euro, Europe's new currency, which would reduce the demand for foreign-currency rates. To compensate, Reuters is scrambling to provide the type of analytics that make Bloomberg so valuable. It became so determined, the feds allege, that it tried to duplicate Bloomberg's formula by re-typing thousands of Bloomberg screens into Reuters' system.

Bloomberg is betting on its uniqueness. "Not everybody needs what we have," says Bloomberg, an ex-Salomon Brothers Inc. partner. "But those that do can't get it anywhere else." Which is why his company may continue to thrive despite its costly closed platform and fixed price. Bloomberg charges a flat \$1,200 a month per terminal and uses dedicated boxes and software that prevent users from mixing Bloomberg data with outside programs. It stopped making the boxes two years ago and has rolled out newfangled machines that double as PCs. It also has created online access.

Users are still limited to Bloomberg applications, but they have more convenience—another buzzword in the battle for desktop real estate. Reuters has already one-upped the competition with a private-label PalmPilot handheld computer from 3Com Corp. One of the first users was BT's Shah. He raves about getting stock quotes on the fly but still can't live without Bloomberg's securities database. "I'll never get rid of Bloomberg," he says. But what will happen when Bridge comes knocking? "It would have to replace something," he says. That's just what Bridge intends to do.

By I. Jeanne Dugan in New York

COMMENTARY

By Kerry Capell

WHAT A 'EURO' COULD DO FOR THE LATIN

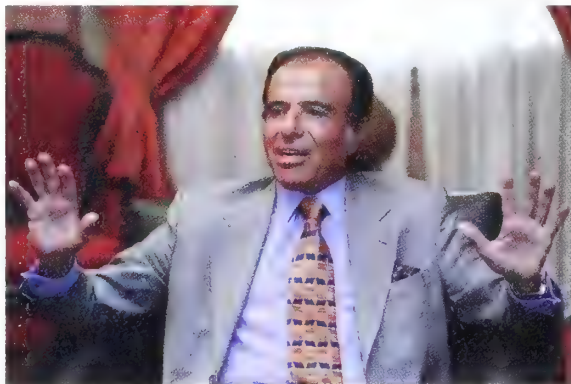
While the world focuses on the euro's imminent launch, South Americans are quietly laying the foundation for a common currency of their own. At a regional summit in June, Argentine President Carlos Menem will renew his call for a single monetary unit for Mercosur, the customs union made up of Brazil, Argentina, Uruguay, and Paraguay. When Menem first raised the idea last December, pundits dismissed it as folly. But they're wrong. Anticipation of the benefits of the euro is already yielding

bership in the European Monetary Union. And since Mercosur's creation in 1991, trade among members has quadrupled, to \$17 billion annually. Because most of the Mercosur currencies are linked to the dollar, they already trade within a close range.

Formalizing a monetary accord will be easier in Mercosur than in Europe, since there are fewer economies to coordinate. And it will offer many of the same benefits. For instance, less exchange rate volatility will increase trade within the region by making it easier for companies to

expand across borders. Improved stability and more competitive exports also will lure new foreign investment.

To be sure, regionally coordinated monetary and fiscal policies are still a long way off. Interest rates are widely divergent—Brazilian three-month yields exceed 27%, while Argentina's are only 6.5%. But Europe has



MENEM: Talking up a single Mercosur currency

Europe a bonanza in the form of corporate restructurings, lower interest rates, and booming stock markets. In the same fashion, a single Mercosur currency—perhaps called the "merco"—could bring economic stability to the region by opening borders and improving trade. Even the Brazilians, whose participation is key, are discussing the possibility. For one thing, adoption of the merco could pressure their procrastinating Congress to cut budget deficits and reduce debt.

Indeed, some of the same forces that are helping get the euro off the ground are evident in South America. For one thing, the region's economies are increasingly converging. Average inflation within Mercosur is now 8.5% down from 275% in 1992. Except for Brazil, fiscal deficits hover close to 3% of gross domestic product—the level required for mem-

bership in the European Monetary Union. And since Mercosur's creation in 1991, trade among members has quadrupled, to \$17 billion annually. Because most of the Mercosur currencies are linked to the dollar, they already trade within a close range. Formalizing a monetary accord will be easier in Mercosur than in Europe, since there are fewer economies to coordinate. And it will offer many of the same benefits. For instance, less exchange rate volatility will increase trade within the region by making it easier for companies to expand across borders. Improved stability and more competitive exports also will lure new foreign investment.

To be sure, regionally coordinated monetary and fiscal policies are still a long way off. Interest rates are widely divergent—Brazilian three-month yields exceed 27%, while Argentina's are only 6.5%. But Europe has the same problem until single-currency fever took hold and interest rates converged. Also problematic are the high levels of domestic and foreign debt in Brazil and Argentina and a lack of common Latin trade rules. relative newcomers to democracy, there's no guarantee that the region's future governments will advocate monetary and fiscal synchronization. common currency would demand. posing monetary union without economic and trade reform would be disastrous.

The Latins have more work to but these concerns should not be barrier to beginning the process. Working toward establishing a merco would keep the region's economies track for sustained growth. Just look to Europe for proof.

Capell follows global currencies from New York.



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COMMENTARY

By Christopher Farrell

THE BUYBACK BOOM IS MOSTLY A BOON

A healthy narcissism thrives in Corporate America, it seems. On Mar. 30, Texaco Inc. said it planned to buy back up to \$1 billion of its common stock, just after completing a \$650 million stock repurchase. General Motors Corp. is buying back \$4 billion of its equity. Intel Corp. just approved another stock buyback program of up to 100 million shares. In 1997, 1,273 companies said that they would spend a mind-boggling \$180 billion repurchasing their own shares, according to Securities Data Co.

Do these deals make economic sense? Or are buybacks just another financial gimmick to boost the stock

from IBM and other companies to thousands of Yahoo's," says Mark M. Zandi, economist at Regional Financial Associates Inc. Money from buybacks, in large part, is fueling the boom in initial public offerings of high-tech, cutting-edge outfits, thus increasing the productivity of the economy.

Companies are saving their shareholders billions in taxes by buying back stock rather than simply in-

creasing the dividend. Dividend payments to taxpaying shareholders are taxed twice: once at the corporate and again at the individual level. In sharp contrast, shareholders who decide to sell their stock are often taxed at the much lower capital-gains rate.

At the same time, owners of 401(k), 403(b), and other tax-sheltered investment plans might prefer a steady stream of dividends. "Shareholders now have more choice about how they receive their cash flow," says Amar Bhilde of the Harvard business school.

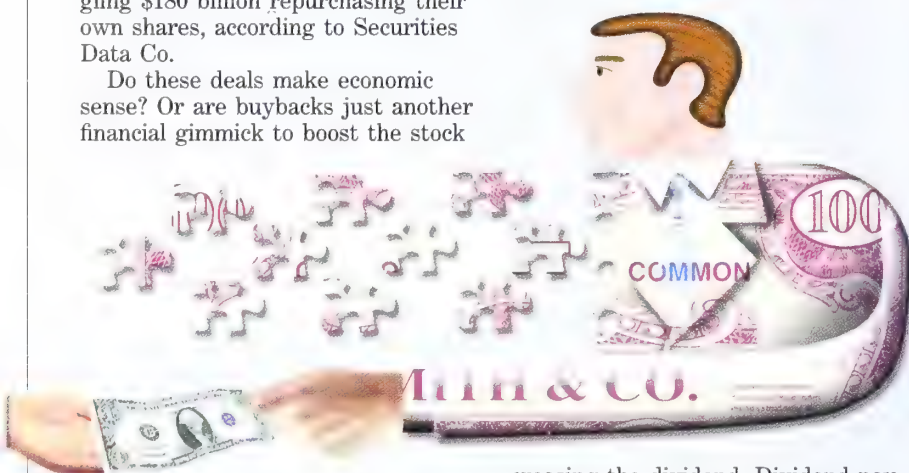
Buybacks tend to boost stock market returns over the long run. Melissa Brown, quantitative analyst at Prudential Securities Inc., studied several thousand large-, mid-, and small-capitalization companies from 1978 through

1996. She compared the stock returns of companies that reduced their shares outstanding by 5% or more with the average return of a peer group. She found that companies with a stock buyback program did better over time. For example, in the group of large-cap companies she found that those with a stock-buyback program gained an average of 21% a year, vs. an appreciation of 15.5% for the group as a whole over the eight-year period. Other studies tend to show a long-term gain on the order of 3% higher for companies that buy back stock, says Steven Kaplan, finance professor at the University of Chicago. Part of the gain, he adds, comes from these companies managing their businesses more efficiently.

BUYING HIGH. Many stock buybacks don't shrink the total equity pool of company. Instead, repurchases are used to offset employee stock options and prevent shareholder dilution. What's more, stock options can enhance employee productivity and, hence, boost stock market returns. Still, aren't companies crazy to buy their stock with the Dow Jones industrial average hovering at record levels? Problem is, market valuations have been stretched for years and, with the benefit of hindsight, past repurchases tend to look pretty savvy today.

To be sure, buybacks are no financial elixir. They are not a replacement for strategies to open up new markets, nurture innovation, and boost profits. Nevertheless, efficiency is not confined to the factory floor. As Paul D. Grangaard, head of corporate finance at the investment banking firm Piper Jaffray Cos., puts it: "Stock buybacks should be a standard part of managing the balance sheet and the company."

Farrell writes about financial economics from America's heartland



price? Shouldn't companies be putting their extra cash in plant and equipment instead? Is the long-term health of U.S. companies—and the economy itself—being sacrificed for a quick buck?

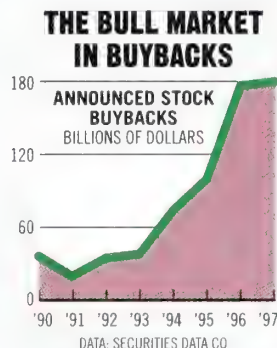
STARTUP CAPITAL. By and large, such fears are misplaced. Buybacks benefit the companies, their shareholders, and the economy. Certainly, investment in plant and equipment is not going begging: In the past five years, total fixed investment has risen at a sound 8.7% annual rate and corporate cash flow has increased at 7.3% per annum, after dividend payments. Says Arvind Sodhani, Intel's treasurer: "We have a strong cash position, and we can fund our growth through cash earned on sales."

Stock buybacks are a way of returning cash to millions of shareholders who may then reinvest their gains elsewhere in the economy where the returns are higher. "With stock buybacks, you get money going

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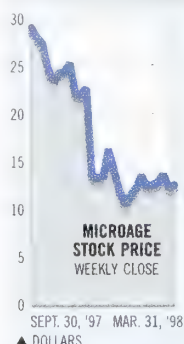
EMPOWERING THE
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BY GENE G. MARCIAL

A BRIGHTER AGE FOR MICROAGE?

The stock chart for MicroAge (MICA) is not for the weak-hearted. It shows steep drops, with shares falling from 30 in October to 10 on Jan. 22—creeping back to 13 on Mar. 31. Earnings at the integrator and distributor of info-tech products and services failed to meet the

NOT FOR THE WEAK OF HEART



Street's expectations, and for the fiscal first quarter of 1998, MicroAge delivered the biggest blow yet: a loss of 28¢ a share, vs. projections of a gain of 36¢. Predictably, many big shareholders headed for the exits. Enter the buyers on bad news.

These contrarians are armed with more than hopes for a turnaround. They're betting the company will split in two: One part will be its distribution business, which sells 20,000 hardware and software products to resellers worldwide. The other is the integration arm, which provides computing solutions to governments, corporations, and schools.

One California investment manager, who started buying after the price fell to 11, figures the two separate pieces would be worth more than MicroAge's current price. Why? If split, each could focus on what it does best, he argues. Others in the same business, he notes, trade at high price-to-sales ratios because they achieve good margins. Given the margins on revenues that rivals achieve, the MicroAge distribution unit could earn some \$50 million, or \$2.50 a share, he figures. MicroAge's distribution business generated sales of more than \$3 billion in fiscal 1997. So this pro reckons the distribution unit is worth 15 to 17 a share, based on the revenues ratios that its peers trade at. The integration operations, which accounted for sales of \$1 billion, could be worth 15 a share, he adds.

Analyst David Grossman of Nations-Banc Montgomery Securities says there is "definitely a possibility" that Micro-

Age will split in two. MicroAge could either spin off or sell its distribution arm, with MicroAge retaining the integration operations. "The company is trailing its peers, and it looks very compelling for MicroAge to split to realize its full potential," says Grossman.

In February, management moved to divide its sales and services divisions into autonomous units with separate management, as part of a restructuring. Some view this as a step toward a split or spin-off. Chairman and CEO Jeff McKeever says MicroAge is "considering all financial options," including a spin-off or sale of its distribution business to enhance shareholder value.

SMILE, IF YOU OWN DENTAL MANAGERS

Nancy Weaver tripled her money in—believe it or not—Columbia/HCA Healthcare. Weaver, who follows health stocks at Little Rock investment firm Stephens, discovered Columbia in 1992 at 12 a share. She sold 2½ years later at 35—way before Columbia's travails.

"There still are niches in health care where just as much money could be made," says Weaver, who is now high on emerging dental-practice-management companies, an undiscovered sector that's ripe for consolidation.

Her picks in the group: Monarch Dental (MDDS), which manages practices for 200 dentists in Arkansas, Colorado, Indiana, Texas, and Wisconsin; and Coast Dental Services (CDEN), which manages 60 centers in Florida, Georgia, and Virginia.

Monarch, now at 16 a share, and Coast, at 27, are the rapidly growing leaders in the \$46 billion dental-care industry, says Weaver. Monarch is an experienced consolidator. She thinks earnings will grow 35% a year for the next three years. She expects it will earn 58¢ a share this year and 80¢ in 1999, vs. 1997's 26¢.

Coast has also been widening its reach, buying practices at 70% of gross revenue. Weaver expects Coast, which plans to acquire a further 15 to 20 offices this year and open 20 new ones, will earn 80¢ a share this year and \$1.10



WEAVER: Monarch and Coast Dental are her tooth picks

next, up from 1997's 55¢. She thinks Monarch stock will have an easy ride to 22, and Coast to 39.

THIS INSURER MAY PAY A PREMIUM

National Insurance Group (NIG) doesn't usually show up on investor radar screens. But it's bound to attract attention soon. Big players, including relative of Italy's Agnelli family who owns a 10% stake, are eager to enhance the value of the stock, which is recovering from a slump that dragged it to in mid-January, down from 11 in late September. It has since risen to more than 10.

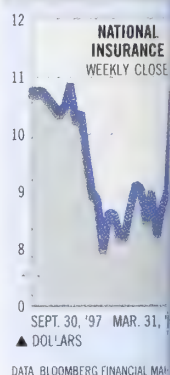
National specializes in policies against floods and other hazards, and in insurance for collateral protection. It's also the business of providing specialized information systems and services—considered to be the company's greatest jewel—to financial institutions.

Whispers are that managements thinking of splitting the company are spinning off the information service, which some pros value at \$100 million, or \$20 a share, based on the price-earnings ratios that other companies in the business trade at. The information unit had sales of \$31 million in 1997. The insurance is worth its book value of \$25 million, or some \$7 a share.

New York investment banker Richard Berman, a National stakeholder, figures the information unit will produce sales of \$45.2 million in 1998. The insurance part, which accounted for \$22 million last year, should bring in only \$19.8 million in 1998, figures Berman. He expects information to produce pretax earnings of \$13 million this year, up from 1997's \$8.8 million. Insurance, on the other hand, is expected to pull in pretax earnings of only \$4.8 million, down from last year's \$6.8 million.

For all of 1997, National earned 7¢ a share, up from 37¢ in 1996. Berman expects National to earn 90¢ in 1998, or \$1.10 to \$1.20 in 1999. National didn't turn calls.

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COLLEGE CASH FROM YOUR RETIREMENT STASH

The old advice was simple: Stash cash for college until your kids graduate, then save like crazy for your own retirement. When 50-year-old empty-nesters who could look forward to hefty corporate pensions were the rule, that counsel worked pretty well.

Look around a PTA meeting today, though, and you'll see lots of parents who've gone gray long before their kids learn multiplication tables. For today's 40-plus parents, college savings compete directly with building a retirement nest egg. So, many financial advisers recommend combining those goals: Pack your savings into retirement accounts, using the tax breaks to help pay for both your kids' education and your golden years. "Put college money in a 401(k), and you'll end up with more for college and more for retirement," says Jeffrey Feldman, a planner at Rochester (N.Y.) Financial Services.

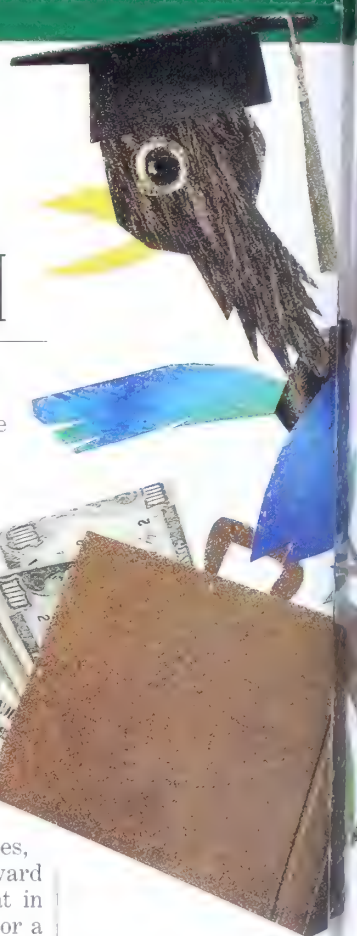
While the tax code makes it easy to build big balances in an individual retirement account (IRA), 401(k), or similar plan, tapping those funds for tuition takes ingenuity. College aid, too, can rise or fall based on where you stash your savings. But with enough planning, parents—especially those who'll be in their mid-50s or older when Junior gets a bachelor's degree—can make retirement accounts serve two purposes. **PROJECTIONS.** First, a word of warning: Don't even think about using retirement funds for education if paying college bills will leave you short for your retirement. Suppose you

need \$12,500 a year, starting at age 48, for college. That \$50,000, plus taxes and a 10% early-withdrawal penalty, will cost your 401(k) \$90,909—and cut your income by \$27,300 every year after you retire. "You've invested in your child's future by sabotaging your own," says Dee Lee of Harvard (Mass.) Financial Educators and co-author of *The Complete Idiot's Guide to 401(k) Plans* (MacMillan General Reference, \$17.95).

So your first step should be a retirement-plan checkup to see if you're saving enough. If your employer's benefits office can't run your numbers, go online, to calculators at [FinanCenter \(www.financenter.com/retire.htm\)](http://www.financenter.com/retire.htm) or *Investors Guide (www.investorguide.com/*

retirement.htm). Software such as Quicken Financial Planner can do more detailed projections.

Once you're set for retirement, you can look at our numbers to see where to stash extra savings for college. Let's say you're putting 6% of your \$80,000 salary in a 401(k) to match your company's match. You figure you can save an additional 4%—\$3,200 a year before taxes, or \$2,080 aftertax—toward college. You can put that in your 401(k), a Roth IRA, or a tax-efficient stock index fund. Assume all the accounts earn 10% before taxes. The charts show what you'll have left if you start saving when your



COLLEGE PLANNING

Comparing Egg-Builders

Parents with an annual income of \$80,000 want to set aside 4% a year for their child's college education. Their federal and state tax rate is 35% (vs. the kid's rate of 20%) and they pay 20% on capital gains (vs. 10% for the child).

Here's how much they would accumulate inside and outside retirement accounts by the time the child is 18:

IF YOU START SAVING WHEN YOUR CHILD IS 6:

401(k)/ROTH IRA POST-AGE 59½	\$46,576
INDEX FUND IN KID'S NAME	\$45,883
INDEX FUND IN PARENT'S NAME	\$41,474
401(k) PRE-59½	\$39,410
ROTH IRA PRE-59½	\$33,004

IF YOU START SAVING WHEN YOUR CHILD IS 12:

401(k)/ROTH IRA POST-AGE 59½	\$16,805
INDEX FUND IN KID'S NAME	\$16,805
INDEX FUND IN PARENT'S NAME	\$15,918
401(k) PRE-59½	\$14,219
ROTH IRA PRE-59½	\$12,288

child is 6 or 12 and pay out—paying taxes and penalties—when he or she is 59½.

Older parents get a break: If they're 59½ when they start to withdraw, they net the most with a 401(k) or a Roth IRA. (Under the 1997 tax law, any IRA can be used without penalty at any age to pay college expenses—a good reason to funnel kids' income into jobs into deductible IRAs.) But the Roth IRA's big break—tax-free earnings—isn't available until age 59½.)

The next best choice is a tax-efficient index fund in your child's name. If you set up a custodial account under the Uniform Gift to Minors Act, you'll have to endure the "kiddie tax" until your child turns 14. The first \$700 of your child's investment earnings will be tax-free, then the next \$700 will be taxed at 15% (10% for capital gains) and the rest will be taxed at your top rate. After child turns 14, they file their own returns; then, they can pay



Older parents get a big break:

If they're 59½ when they start to draw down a Roth IRA, their withdrawals are tax free

4,250 in earnings from tax. An account that started for a year-old child altogether, matching the child's performance—while an account that grows gets nicked. On the downside of a custodial account: You surrender control of the cash when your child reaches 18 or 21. If you're under age 59½, you'll pay a 10% penalty (tax) for early 401(k) withdrawals. Even so, a 401(k) might outperform a 529 account if you have to save or if your non-qualified funds generate more income than this hypothetical index fund. Investing in a Roth IRA is the choice if you'll need to draw earnings early. The effect of this takes into account another "tax"—one imposed by college financial-aid rules. Many middle- and

upper-income parents assume they won't qualify for aid. In fact, a family with one college-bound student can often get tuition help if it has income below \$125,000 and modest assets, says John Roche, a certified financial planner and aid specialist in Hartsdale, N. Y. With two or more kids in school, "it's hard not to qualify," Roche says.

LOAN STRATEGY. A 401(k)-based college fund is a mixed blessing at the financial-aid window. On the plus side, the formula for federal (and most state) aid doesn't expect you to spend retirement assets on college. If you've earmarked \$50,000 in your 401(k) for college rather than setting up a separate account, you can

qualify for \$3,000 more federal aid. But suppose you draw \$12,500 from your 401(k) to pay first-year bills. When you apply for sophomore aid, that will show up as income—and mean about \$3,750 less aid.

So how do you tap your 401(k) or IRA with the least consequences? With a 401(k), you can take a loan: 75% of employers let savers borrow half their 401(k) balance, up to \$50,000. But experts frown on 401(k) loans because they slow your fund growth. Such loans must be repaid fast: If you borrow \$12,500 a year, by the time Junior's a senior, you'll be shelling out \$11,000 in annual payments. And 401(k) loans have a doomsday feature: If you leave or

lose your job, your loans are due in full immediately.

A smarter strategy is to borrow elsewhere. A home-equity line of credit, with a 15-year term and tax-deductible interest, is the best deal. Banks also offer a federally subsidized package called PLUS—Parent Loans for Undergraduate Students—to help parents pay their share of college costs. PLUS loans last 10 years, with interest capped at 9%.

Wait a minute—what's the point of borrowing if you've spent years building a college fund inside your 401(k)? In high-finance terms, you're using a "bridge loan"—funds to tide you over until it's cheaper to tap your retirement account. If you're in your 50s when your child enters college, you can use a home-equity loan to pay your share of school bills. Sure, you'll pay interest—but it will cost less than what your 401(k) funds can earn. And you can start tapping your 401(k) to pay off the home-equity loan after you turn 59½ with no penalty and no financial-aid hit.

That strategy won't work for everyone. Your 401(k) plan may not allow large enough contributions to build both a retirement kitty and a college fund. Your house may already be leveraged to the hilt. Psychologically, you may need the comfort of seeing separate accounts for education and old age. But with a double savings challenge looming before you, it might be hard to overlook the extra oomph that 401(k)s and other retirement accounts can bring to your net worth. True, you'll need some financial skill to tap the funds. But an extra dose of wisdom is one of the advantages older parents can bring to the party. *Mike McNamee*

FOR CHEAP SCHOOLING, GO NORTH

Nefra Faltas faced a choice in her last year at the Potomac School in McLean, Va.

Would she spend her next four years at Oberlin College, the University of Virginia, or the University of Toronto? She leaned toward Toronto. "The campus seems very American, but with a lot more cosmopolitan flavor," says Faltas, now a first-year pre-med student at UT. The clincher: With all costs in, her first-year bill at Oberlin would have been about \$29,000; at U. Va., \$11,800; and at UT, just \$11,200.

For U.S. citizens staggered by higher education costs, Canada's 50 or so undergrad universities may be as welcome as a northern breeze. They are inexpensive as a matter of government policy. And while non-Canadians may pay up to three times what locals do, they'll still save a bundle compared with private U.S. colleges or top-flight state schools—especially with the U.S. dollar strong against the Canadian loonie. **FAMILIAR.** The pluses of getting some northern exposure go beyond dollars. Familiar enough culturally—and near enough geographically—to appeal to students reluctant to venture too far abroad, the schools are nonetheless foreign. The highly diverse student populations reflect Canada's role as a magnet for immigrants. Then there's Quebec, where you can study at an English-speaking school such as McGill University while exploring a unique French culture.

Wherever in Canada U.S. students go, they'll find differences from home. "People

really are much more polite," says Benjamin Moerman, a political philosophy grad student who came to UT after Harvard Divinity School. Crime is often less of a worry, even in big cities. Canadians may also be more focused academically. One reason: They home in on a major early in high school to prepare for mandatory achievement tests needed for university admission. The tests measure actual academic mastery rather than aptitude.

Athletic programs, meanwhile, are rich—think wide-field football and curling—but not big-time, as in larger U.S. schools. Only Simon Fraser University in Vancouver has teams competing with U.S. schools in the National Association of Intercollegiate Athletics. Athletic scholarships, too, are rare in Eastern Canada.

Costs vary widely. British



AMERICAN ABROAD: Faltas at the University of Toronto

Columbia lets schools charge heavily for foreigners. So a U.S. student at the University of British Columbia would pay about \$16,000 a year. By contrast, the University of Windsor, near Detroit, offers a break just for U.S. students, charging about \$7,700.

As for admissions standards, highly selective UT and McGill demand A or B+ av-

erages and high class rankings. Generally, Canadian schools give less weight to Scholastic Assessment scores, which aren't even required of Canadians.

Thanks to the Net, research is easy. Most colleges and universities post websites. And *Maclean's* newsweekly, publishes listings of schools each fall (www.macleans.ca). Canada's Foreign Affairs Dept. also has such info as its requirements (www.cdnemb-washington.org/study).

While weighing Canadian education bears in mind that unfamiliar alma mater on a résumé may be a plus when entering a career at home. Even Mount Allison University, New Brunswick, in 41 Rhodes scholars among its grads, may draw blank looks from U.S. employers. It's for adventure-seekers, budget-minded students, a Canadian education may be the bargain on the market. *Joseph Pal*

COLLEGE PLANNING

Canadian Options

SCHOOL	TUITION & FEES	ROOM & BOARD	APPLICATION DEADLINE	FEATURES
McGILL UNIV., MONTREAL www.mcgill.ca	\$6,575-9,416	\$3,320-4,488	Jan. 15	Top-rated research institution
MOUNT ALLISON UNIV. SACKVILLE, NEW BRUNSWICK www.mta.ca	\$5,350*	\$3,822*	Aug. 1	Strong liberal arts & sciences school
SIMON FRASER UNIV., VANCOUVER www.sfu.ca	\$3,920	\$1,540-1,960	Apr. 30	Links to Asia; athletic teams compete in U.S.
UNIV. OF ALBERTA, EDMONTON www.ualberta.ca	\$5,180	\$2,450	Mar. 1	Strong in agriculture and forestry
UNIV. OF TORONTO, TORONTO www.utoronto.ca	\$6,300-8,400*	\$840-4,200*	Mar. 1	Leading urban school with downtown campus

* 1997-98

DATA: UNIVERSITIES

FE INSURANCE: DROWNING FEES

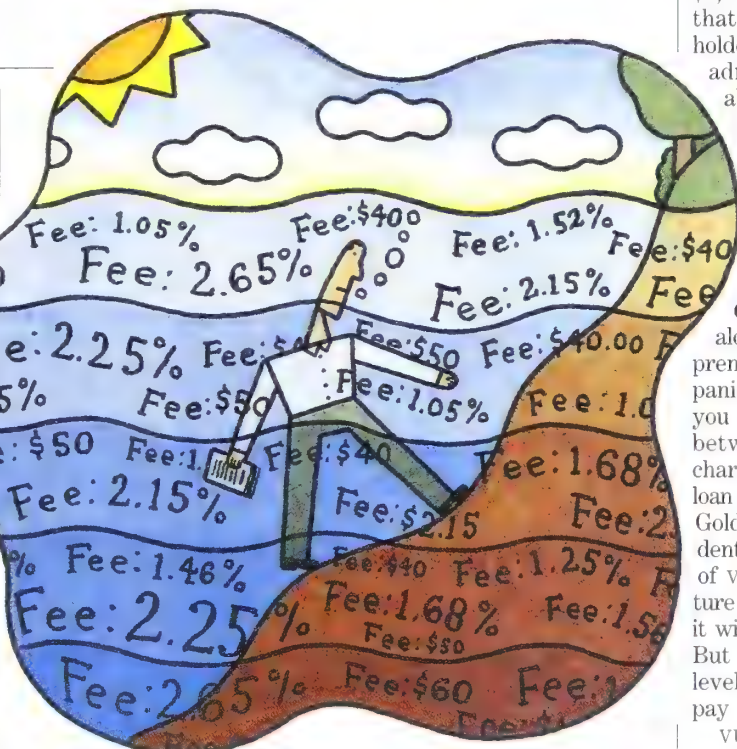
able universal life insurance is the fastest-growing product in the life-insurance industry.

One 20% of new policies today, 7% just five years ago. Consultants are snatching it because it's one of the few ways to get 401(k) plans and individual retirement accounts, to invest in mutual funds and get tax-free growth. Why does financial planner Whitehead of Franklin, refer to VUL as a "suck-ly"? It's simple, the answer is the fees. They are so clogging that in many cases even insurance agents don't understand them. Many are buried in the fine print of a prospectus, and others are lumped together as miscellaneous material.

SMART MONEY

Like matters worse, comparing shopping is almost impossible because each company's fees and terms are different. Experts estimate it takes 10 to 20 years to even after fees, depending on how much you pay for the policy each year and the underlying mutual fund perform. If you don't have a long investment horizon, it is almost a sure way to lose money. Says Bill Fleming, an insurance specialist in New York & Lybrand's Hartford office, "The best exit strategy for a variable universal life policy is to sell it."

Like term insurance, a VUL policy has no payoff unless you cash it out. The value over time. The policy has to fork over



big premiums for a number of years—and meanwhile hope your funds perform well—before the policy becomes "fully funded." That's the point at which there's enough money

in the account to pay the insurance and fees. But if your funds fare poorly or policy costs go up, you can wind up paying premiums for longer than the original projections suggest.

HUGE PREMIUMS. Take a \$1 million policy from Equitable Life, the leading marketer of VUL, for a 35-year-old healthy, nonsmoking man. The policy is similar to products offered by other life insurers, such as Prudential, Nationwide, and Northwestern Mutual. The premium is \$9,540 a year for 10 years for the policy to become fully funded. This assumes that the funds invested earn 10% annually net of management fees. By comparison, a \$1-million level premium term policy would

cost \$920 a year for 20 years.

Enormous premiums are required for VUL because a large portion of the payments goes toward fees, rather than the policy itself. First, the insurer deducts about a 4% sales charge, also called a

"load," from every premium, a process that instantly cuts the \$9,540 payment by \$353. Then there's a life-insurance cost—in this case, it's 18%, or \$1,685, in the first year, and that goes up as the policyholder gets older. A first-year administrative fee runs about \$300, followed by a permanent monthly expense of \$6. You can also count on an ongoing mortality expense fee, a state premium tax, and a fund management fee.

CASHING IN. The fees alone reduce your first-year premium by 17%. Many companies also tack on levies if you want to transfer money between funds, and most charge you for taking out a loan against the balance. Jerry Golden, executive vice-president of Equitable and creator of VUL, admits the fee structure is too complex and thinks it will eventually be simplified. But he justifies the high fee levels by saying, "We have to pay our agents something."

VUL is an especially bad deal if you need to cash in the policy within 10 to 15 years. That's because you'll be hit with a large surrender fee. In the Equitable example, if you cash in the policy after one year, you're subject to a surrender fee of \$5,576. That means you'll get back only

Deconstructing a Policy

The following illustration is based on a \$1 million variable universal life insurance policy for a 35-year-old male nonsmoker. It assumes annual premiums of \$9,540 for 10 years and annual investment gains of 10%.

YEAR	PREMIUMS PAID	ACCOUNT VALUE*	VALUE OF CASHED-IN POLICY**	ANNUAL RETURN ON INVESTMENT
1	\$9,540	\$7,961	\$2,385	-73.2%
5	47,700	47,963	41,298	-2.2
10	95,400	119,354	114,129	4.9
15	95,400	165,526	165,526	6.6
20	95,400	231,793	231,793	7.0

*After fees, plus 10% investment gain **After surrender charge, which starts at \$5,576 in Year 1 and decreases every year until it disappears in Year 15

DATA: EQUITABLE LIFE, CONSUMER FEDERATION OF AMERICA

\$2,385 from a \$9,540 contribution plus a 10% investment gain. You'd still be under water until year 15, when the surrender charge disappears.

In an analysis of the Equitable policy, James Hunt, an actuary and consultant to the Consumer Federation of America (CFA), showed how all the fees make it difficult to achieve stellar investment returns. He concluded that by cashing in the policy in the fifth year, it would lose 2.2% of its value on an annualized basis. Even if you held it for 20 years, it would gain only 7.0%. "Buying term insurance and investing the difference would

be more profitable," Hunt says.

The surrender fee underscores why VUL is, at best, a long-term investment. As Equitable's Golden says, "You're not supposed to cash in life insurance. Your goal should be to hold it." Still, more than 50% of all people who buy VUL cash in their policies before the surrender fee expires, according to industry estimates. This suggests agents are marketing the policies to the wrong people. But they have a strong incentive: commissions of at least 55% of the first year's premium and 4% for the next 10 years.

A big selling point is you

can borrow against your cash balance and not have to repay the loan while you're alive. The loan amount will be deducted from the money paid to your heirs. What often isn't made clear is that when you take the loan, you have to pull a matching amount of money out of the stock mutual funds in the policy and put it into a money-market fund as collateral. This limits the ability of the policy to earn enough to cover the annual insurance cost and reduces the odds of breaking even on the fees.

Despite drawbacks, VUL can benefit a narrow group of people. The ideal candidate is

someone who has a high net worth, needs a tax shelter, and is willing to shell out big bucks up front to capture the benefits of compounded growth, and doesn't need the money anytime soon. If you fit this profile and are interested in VUL, a good option might be a policy from Annuity Life (800 552-3553), which offers a low-load option in 10 states and expects to have more available in the last two, New York and New Jersey, within the year. Before you agree to any contract, get the CFA's (387-6121) to do a cost analysis for \$40. This is a cheap way to avoid being sold a sucker policy. *Adele Mahoney*

SEXY STEEL STOCKS? DON'T LAUGH

Steel stocks may not have the allure of high-tech shares, but an obscure segment

known as steel processing might be worth a look. Despite troubles last year, the sector's growth has Wall Street excited. "There are real opportunities, but the sector is poorly tracked," says Michelle Galanter Applebaum, managing director of Salomon Smith Barney in Highland Park, Ill.

The growing prominence of these so-called metals-service centers reflects the steel industry's increasing specialization. Service centers distribute commodity steel, but lately several have moved into the more profitable business of making highly finished steel for use mostly in cars, appliances, and construction. They are taking over these higher-profit-margin functions from steelmakers, which prefer to avoid the outlays associated with capital-intensive, advanced processing. So while the processing segment has enjoyed strong sales growth for many years, its profit

margin has lately been rising as well—to the 8% region, from the typical 4% for distributors, analysts say.

At least 14 processors with a market capitalization in excess of \$5 billion now trade publicly compared with two just 10 years ago, says Kenneth Hoffman, an analyst at Prudential Securities. Of the

companies that have good records of profitability—and savvy expansion plans (table). Two on Wall Street's pick lists are Reliance Steel & Aluminum and Gibraltar Steel. Reliance, a Los Angeles processor and distributor with annual sales gains of 20% to 30% and a record of smart acquisitions—10 since its 1994 IPO—has convinced many of its growth potential.

Gibraltar's recent investments, like those of Reliance, have won praise from analysts. A leader in cold-rolled steel, it invested last year in a rolling mill in Cleveland that it says will

Cleveland distributor supplies General Motors, caught off guard by a surge in cheaper imports which had a lot of high-priced steel in its inventory.

ROUGH PATCH. Barometer hunters might find that Worthington Industries may be a gander. Worthington's first processor to go public in 1971, ran into a rough patch in the early 1990s after about plans to invest in a steel plant. It recently invested in a vanishing facility and a processing plant. "They're putting a lot of money into new plants.... If they can turn that into profitability, it



HEAVY METAL: Growth play

14, nine have grown an average of 20% annually in the past three years—and are trading at an average price-earnings ratio of about 12, well below the Standard & Poor's 600 SmallCap Index average of 23.

Analysts recommend that investors choose top-tier com-

panies that have good records of profitability—and savvy expansion plans (table). Two on Wall Street's pick lists are Reliance Steel & Aluminum and Gibraltar Steel. Reliance, a Los Angeles processor and distributor with annual sales gains of 20% to 30% and a record of smart acquisitions—10 since its 1994 IPO—has convinced many of its growth potential.

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Steel Band

COMPANY	STOCK PRICE*	52-WEEK HIGH	P-E RATIO
CASTLE METALS	23 1/2	26 1/2	10
GIBRALTAR STEEL	21 1/2	28	13
RELANCE STEEL & ALUMINUM	38 1/2	38 1/2	10
RYERSON TULL	19 1/2	20 1/2	11
SHILOH INDUSTRIES	21 1/2	23 1/2	11
WORTHINGTON INDUSTRIES	17 1/2	20 1/2	11

* Mar. 30, 1998 ** Based on estimated 1998 earnings

DATA: BLOOMBERG FINANCIAL MARKETS

boost annual revenues, now at \$450 million, as much as \$85 million in three years.

Investors should remember, however, that the business is highly sensitive to commodity-steel price fluctuations. Indeed, last year the industry saw a high-profile slump when Olympic Steel, a

stock will have plenty of room to grow," says Ralph Wiegman, chief investment officer of Acorn Trust, a \$3.7 billion fund in Chicago that owns \$23.3 million of Worthington stock. And growth at a reasonable price—is what makes processors promising. *Johanna Knapp*

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"These are triumphant times for Latin America. Inflation is at a 50 year low, trade barriers have been slashed, and capital markets liberalized. Business is roaring." As President Clinton's Special Assistant for Inter-American Affairs, **Richard Feinberg** witnessed three years of Latin America's historic transformation at close range. Feinberg says Asia's economic crisis "illuminates the gains in Latin America. Development is more than investment rates: Political development also matters, and there Latin America excels. It's wall-to-wall democracy."

The 1998 Annual Business Week Latin America Summit was a wall-to-wall celebration of a region's remarkable success. Business leaders and heads of state alike cheered the changes that have swept Latin America.

Argentina has seen one of the hemisphere's most dramatic makeovers. **President Menem** told the summit, "We have transformed the Argentine state. We have deregulated the market. We have started an economic opening and transformation. We have restructured our public debt. Argentina has been brought to political stability with a rational, predictable economy." Menem's Argentina created more than one million new jobs in 1997, yet held inflation at just one-tenth of one percent.

Freshly returned to Mexico after three years as his country's ambassador in Washington, **Jesús Silva-Herzog** says the vocabulary of Latin America has changed. "Protection. Subsidies. Government intervention: These words are gone!" Brazil's Secretary General for External Relations, **Sebastião do Rego Barros**, calls it "a silent and peaceful revolution. Where authoritarianism and uncertainty ruled, democracy and stability now prevail. It is a new Latin America."

Lessons Learned, Learning Applied

How did it happen? Latin America learned the hard way, but it learned. **Dr. Jorge Dominguez**, director of the Weatherhead Center for International Affairs at Harvard University, recalls that "President Menem attempted to command the economy and govern by decree. That did not work. So he took a different approach. This process of learning has occurred across the continent."

"We are not fazed by what is happening in East Asia," declares an exultant



"Latin America and the Caribbean are quickly approaching the type of consumer-driven telecommunications environment we are familiar with in North America."

Dan Hunt
president, Caribbean
and Latin America,
NORTEL

BusinessWeek
EXECUTIVE PROGRAMS

MEASURING EMERGING MARKETS



David Hirschmann
managing director,
western hemisphere
affairs, international
division, U.S. Chamber
of Commerce

"The international investment community demands a lot from these countries," says **David Hirschmann**,

managing director of the Association of American Chambers of Commerce in Latin America and managing director for western hemisphere affairs at the U.S. Chamber of Commerce. "They must achieve macro-economic stability

together with political stability, the rule of law, a predictable regulatory environment, intellectual property protection, and the right rules for foreign investment. Once all that is in place they must also have an attractive domestic market, access to other markets through economic integration or free trade arrangements, an infrastructure that works and a workforce with satisfactory levels of preparation and productivity. I don't think there is any country in Latin America that gets an "A" in all of these factors, but most get "A"s in some, and every country's report card is looking better every year."

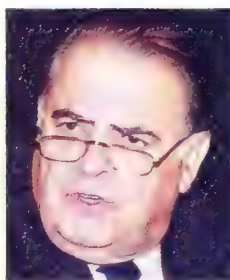


Hon. Carlos Saúl Menem
President of the
Argentine Republic

Two national presidents attended the first BUSINESS WEEK LATIN AMERICA SUMMIT, **President Menem** of Argentina and **President Figueres** of Costa Rica. Their countries are two of Latin America's most successful: Argentina has wiped out inflation with its firm peg to the dollar, and Costa Rica's per capita income is two-to-three times the Latin American average.

"A nation organizes itself into a state to provide essential services to the people. The essentials are justice, healthcare, education, and security. All the rest necessarily must be transferred to the private sector in an open, market economy. This is what we have deemed in Argentina. This is the only possible way ahead, the only solution to the problems of Latin America." - *President Menem*

"We have moved from inward-looking economies with a lot of state intervention, toward a much more intelligent mix, with the strength of a vigorous private sector. A new Christopher Columbus is arriving in Latin America, not in the form of a person, but in the shape of a continental market: a Free Trade Area of the Americas that will unite us all as a family." - *President Figueres*



"Looking at the crisis in Asia I become even more convinced of the need for openness, cooperation, and economic integration."

Hon. Enrique V. Iglesias
president,
The Inter-American
Development Bank

Antonio Vives, deputy manager for infrastructure, financial markets and private enterprise at the Inter-American Development Bank. "Latin America can say to the Asians, 'See! if you had done what we did, you would not be in this predicament.'" Vives' boss, IDB President **Enrique Iglesias** says. "Asia's travails have come as a big shock. We looked to Asia as an example. But Asia's crisis revolves around bank policies and imprudent investments. It is a crisis of mismanagement. The big improvement that I see in Latin America is exactly that: the management is better at all levels, public and private. Everyone is aware that things should not be managed imprudently."

The Banks Are Better Here

"Latin America's banks are in much better shape than Asia's," says **Francisco Gros**, managing director and chairman of Morgan Stanley Latin

The 1998 Business Week Latin America Summit



"Latin America's banks are in much better shape than Asia's, much less leveraged"

Francisco R. Gros
managing director
and chairman of
Morgan Stanley
Latin America



"With privatization you get the business, the asset, and the market share, all in one go."

Luciano Respini



Hon. José María Figueres Olsen
President of the
Republic of Costa Rica



the
tries have
formed,
as had to
form, too."

McCarter
nt and CEO,
I Electric
merica

America, twice the president of the Central Bank of Brazil. "Our banks are much less leveraged. The Latin economies' banking systems are not the Achilles' heel that they turned out to be in Asia."

"Latin America has seen volatility due to the Asia crisis," says **Claudio Loser**, director, western hemisphere of the International Monetary Fund, "but we have also seen rapid recovery thanks to the superb policy response from the economic authorities of Brazil, Argentina, Mexico and others. Their effective response is a tribute to the new generation of policy-makers in the region."

Gone South - And Loving It

"This region has turned the corner," says Hewlett-Packard Latin America President **Rui G. da Costa**. "HP's Latin America business is doubling every two years. Latin America is moving towards client-server systems. Without the latest information technology, their companies can not compete globally."

The largest foreign companies active in the region are generally not newcomers. But that is not always a competitive edge. "General Electric has been in Latin America more than 100 years," says GE Latin America president and CEO **John McCarter**. "As the countries transform, we've had to transform, too. We were a set of far-flung separate General Electrics. We have had to restructure and globalize all those operations."

"In telecommunications, Latin America and the Caribbean are quickly approaching the type of consumer-driven telecommunications environment we are familiar with in North America," says **Dan Hunt**, president, Caribbean and Latin America, NORTEL. "Ownership rules are liberalizing, subsidies are disappearing, and competition is either present or on the way." NORTEL now often finds itself simultaneously installing telecommunications systems for more than one competitor in the same market. Says Hunt, "The global players are arriving and you also see local players forming alliances. These new multinational groups can become global operators themselves."



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ll; executive
sident, Latin
t, Whirlpool
ation; president,
mber of
rce, São Paulo

THE NEIGHBORS GROW NEARER

"We are seeing a revolution in the way U.S. business people view the Latin American markets, thanks to the new mobility of goods and capital. The U.S. is awakening to the fact that here in Miami, we are closer to eight countries in South America than we are to San Francisco, and also closer to more than 12 countries of Central America and the Caribbean than we are to Chicago."

Hon. George Muñoz, president and CEO,
U.S. Overseas Private Investment Corporation (OPIC)



"Look at the new **GATS**: seventy countries have signed this **General Agreement on Trade in Services** opening a global market for telecommunications, information technology, banking, insurance, and securities trade. Most of the Latin American countries have signed. It means nearly \$60 trillion in securities, insurance premiums, and bank lending can now flow more freely across national borders. This is a huge boost for the international business environment."

Jan S. Jobe, president, Principal International, Inc.;
chairman, International Insurance Council



"Today, the risk of hesitating while your competitor makes port in South America is probably greater than the inherent risk of entering a new market in the region. Latin America offers American companies vast potential for growth. The U.S. Postal Service has developed 'Global Delivery Services' to help U.S. firms enter or expand across these evolving markets. This is a very large initiative: the Postal Service Board of Governors has approved \$500 million to create six dedicated international service mail centers in Miami, Dallas, Los Angeles, New York, Chicago, and San Francisco. Our commitment will assist U.S. firms to deliver to the world."

James F. Grubiak, vice-president, international business,
The United States Postal Service





"The number one cause of failure among foreign firms in Latin America is the gap between corporate cultures."

César Souza
senior vice-president,
Odebrecht of
America, Inc.

community. The number one cause of failure among foreign firms in Latin America is the gap between corporate cultures."

Issues of culture and popular expectation may shape the business future of the region. "Public opinion research confirms a startling transference of responsibility for change from the governments to the private sector," says **Beatrice Eugenia Rangel**, senior vice-president, corporate strategies at Venezuela's Cisneros Group of Companies. "Seventy percent of the people now place their faith in economic growth – not in government policy. Our people now expect and demand that

The Latin American Corporate Citizen

Latin American multinationals are springing up in many industries. Local electronics retailers in Colombia and Ecuador now quake at the arrival of CARSA, a powerful Peruvian competitor. All across the region, when big projects are launched, Brazilian construction giant Odebrecht is a likely bidder. "Winning the bid is easy," says Odebrecht senior vice-president **César Souza**. "The challenge begins when the winner must enter a new local business

No MORE SANCTIMONIOUS SELF-RIGHTEOUSNESS



Hon. Mickey Kantor
U.S. Secretary of
Commerce and U.S.
Trade Representative
in the first Clinton
Administration

"This year, trade will account for more than a third of the U.S. economy, more than \$2.2 trillion. The U.S. is the number one importing and exporting nation in the world, and Latin America's more stable, more prosperous, growing economies are big new markets for U.S. goods and services.

But it will work only if Americans have the courage and leadership to drop our sanctimoniousness and self righteousness. We must be willing to work with others."

the business community deliver progress in the form of a rising and more equitably shared standard of living. They are not yet certain whether that delivery will take place on time or to the right addresses." Rangel is herself an example of the shift in direction in Latin America: a prominent official in past Venezuela governments, now a prominent corporate executive. She warns that the outcomes of eleven national elections to be held in Latin America during the next three years ride largely on the civic performance of the private sector. "Relapses," says Rangel, "cannot be ruled out."



"Latin America's people now expect and demand that the business community deliver progress."

Beatrice Eugenia Rangel
senior vice-president,
corporate strategies,
Cisneros Group of
Companies

BusinessWeek
EXECUTIVE PROGRAMS

The 1998 Business Week Latin America Summit

POLL RESULTS

Two hundred ninety-executives active in Latin America were invited to anonymously vote their opinions during THE BUSINESS WEEK LATIN AMERICA Live polling system piloted by Meridia Interactive. Complete poll results the Business Week website at www.businessweek.com/execprog/latin

Latin America's economic reform will...

Continue at its rapid pace:
Continue, but slower
Falter:

Asia Crisis Impact Latin America:

None:
Small devaluations:
Large devaluations:
Very serious economic effects:

Latin American governments may 'go too far' reducing the economic role of the state:

Yes: 33%
No: 63%
Don't know: 4%

1998 progress toward hemispheric free trade:

Rapid advance w/ U.S. in leading role:
Rapid advance in Latin America, but U.S. absent:
Little advance in 1998:

Where I do business in Latin America, corruption is a continuing problem:

Is a declining problem:
No longer exists:
Never touched my business:

I have been asked for a bribe (or similar corrupt practice):

Yes:
Never:

Wireless on-hall polling by Meridia Interactive (616) 260-0000

FROM GOVERNOR TO PRESIDENTIAL CANDIDATE



Hon. Vicente Fox
Governor, State of
Guanajuato, Mexico;
Candidate for the
Office of President
of Mexico

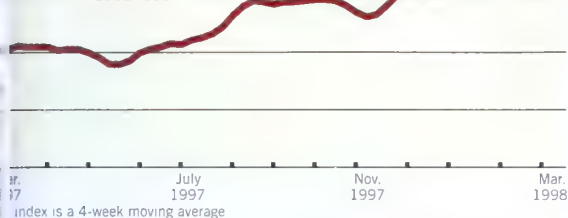
When **Vicente Fox** agreed to speak at THE BUSINESS WEEK LATIN AMERICA SUMMIT he was merely the popular governor of booming Guanajuato State. By the time he arrived in Miami this former CEO of Coca-Cola of Mexico had declared his candidacy for president.

Business Week Index

PRODUCTION INDEX

Change from last week: 0.0%
Change from last year: 4.3%

PRODUCTION INDEX
Mar. 21=130.9
1992=100



The production index was unchanged in the week ended Mar. 21, while the adjusted index was up a full 1%. The seasonally adjusted figures showed a 5.1% gain in truck production this week, and *Ward's Automotive Reports* noted that exports rose 53.9% in 1997, with General Motors Corp. posting the biggest truck shipments. Increases in the output of coal, steel, autos, oil, lumber, and freight traffic were also strong. Electric power posted a 3.1% decline.

Source: Index compiled by The McGraw-Hill Companies

PRICING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
PRICES (3/27) S&P 500	1095.44	1099.16	44.7
LIBOR BOND YIELD, Aaa (3/27)	6.69%	6.66%	-12.3
SUPPLY, M2 (3/16) billions	\$4,123.2	\$4,118.9r	6.7
CLAIMS, UNEMPLOYMENT (3/21) thous	313	309r	0.3
MORTGAGE APPLICATIONS, PURCHASE (3/27)	222.2	234.1	-13.6
MORTGAGE APPLICATIONS, REFINANCE (3/27)	1,297.1	1,421.4	140.9

S: Standard & Poor's, Moody's, Federal Reserve, Labor Dept., Mortgage Assn. (Index: March 16, 1990=100)

INTEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
BAL FUNDS (3/31)	5.88%	5.41%	6.18%
COMMERCIAL PAPER (3/31) 3-month	5.50	5.48	5.71
MORTGAGES OF DEPOSIT (4/1) 3-month	5.60	5.58	5.70
MORTGAGE (3/27) 30-year	7.17	7.15	8.21
TABLE MORTGAGE (3/27) one-year	5.77	5.76	6.02
(3/27)	8.50	8.50	8.50

S: Federal Reserve, HSH Associates, Bloomberg Financial Markets

Data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense. nt. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

INSTALLMENT CREDIT

Apr. 7, 3 p.m. EDT ▶ Consumers borrowed \$4 billion more in new installment credit in February. That's the latest forecast by economists surveyed by Standard & Poor's MMS, a division of The McGraw-Hill Companies. Household debt jumped \$2.9 billion in January. Installment credit growth has slowed over the past year by a steep easing in revolving debt, but includes credit cards. Less borrowing, along with the strong gains in personal income, means that the ratio of installment credit to disposable income has fallen to 20.3% so far in the first quarter, down from a record 20.8% in October,

1996. Moreover, consumers are managing their debt loads better. According to the American Bankers Assn., the percentage of credit-card accounts that were delinquent 30 days or more fell to 3.04% in the fourth quarter, from a record 3.72% a year earlier.

PRODUCER PRICE INDEX

Thursday, Apr. 9, 8:30 a.m. EDT ▶ Producer prices for finished goods likely fell by 0.1% in March, says the S&P MMS median forecast. Plunging oil prices and pressure from cheaper imports likely offset expected increases in food prices and some other goods. Excluding food and energy, core prices were probably unchanged in March. In February, the total producer price index

fell 0.1%, its fourth consecutive decline, while the core index increased 0.1%. Over the past year, the total PPI has fallen 1.7%, mostly because of dropping oil prices. The core index is virtually flat.

NEW UNEMPLOYMENT CLAIMS

Thursday, Apr. 9, 8:30 a.m. EDT ▶ Initial claims for state unemployment insurance benefits probably totaled about 310,000 for the week ended Apr. 4. Filings had declined to as low as 299,000 in the first week of March and then settled into the 310,000 range for the rest of the month. That's still a low level for jobless claims—and another indication of the extreme tightness in the labor markets.

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (3/28) thous. of net tons	2,246	2,250#	4.7
AUTOS (3/28) units	120,775	120,579r#	11.2
TRUCKS (3/28) units	147,379	145,402r#	46.7
ELECTRIC POWER (3/28) millions of kilowatt-hrs.	59,649	61,674#	4.7
CRUDE-OIL REFINING (3/28) thous. of bbl./day	14,601	14,734#	2.2
COAL (3/21) thous. of net tons	21,902#	20,171	-1.4
LUMBER (3/21) millions of ft.	481.6#	475.0	-5.6
RAIL FREIGHT (3/21) billions of ton-miles	27.0#	25.4	-0.7

Sources: American Iron & Steel Institute, *Ward's Automotive Reports*, Edison Electric Institute, American Petroleum Institute, Energy Dept., WWPAl, SFPAl, Association of American Railroads

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (4/1) \$/troy oz.	301.000	299.250	-14.3
STEEL SCRAP (3/31) #1 heavy, \$/ton	135.50	135.50	-0.7
COPPER (3/27) ¢/lb.	82.4	83.8	-31.2
ALUMINUM (3/27) ¢/lb.	69.5	69.8	-12.4
COTTON (3/28) strict low middling 1-1/16 in., ¢/lb.	67.44	67.78	-3.2
OIL (3/31) \$/bbl.	15.33	15.40	-23.2
CRB FOODSTUFFS (3/31) 1967=100	229.17	230.47	-6.6
CRB RAW INDUSTRIALS (3/31) 1967=100	300.51	304.07	-11.1

Sources: London Wednesday final setting, Chicago market, *Metals Week*, Memphis market, NYMEX, Commodity Research Bureau

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (4/1)	133.75	129.06	122.72
GERMAN MARK (4/1)	1.85	1.83	1.67
BRITISH POUND (4/1)	1.67	1.67	1.64
FRENCH FRANC (4/1)	6.21	6.13	5.63
ITALIAN LIRA (4/1)	1826.8	1800.0	1659.0
CANADIAN DOLLAR (4/1)	1.42	1.41	1.39
MEXICAN PESO (4/1)	8.505	8.517	7.939
TRADE-WEIGHTED DOLLAR INDEX (4/1)	111.5	109.6	104.6

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars. Trade-weighted dollar via J.P. Morgan

This Week, Online

Business Week presents frequent live conferences and chats on America Online—your opportunity to ask questions about timely topics.

Sunday

Now's the time for last-minute tips from tax whiz Jim Vonachen, in an event presented with AOL's new WorkPlace Weekend. **Apr. 5 9 p.m. EDT in BW Online's Conference Room**

Thursday

How do you spot values in today's market? Martin J. Whitman of Third Avenue Funds tells us how. **Apr. 9 9 p.m. EDT in BW Online's Conference Room**

B-Schools

Two more chats for MBA wannabes about campus life at the top B-schools. **Apr. 7: Duke**
Apr. 9: Berkeley
8 p.m. EDT in the BW Online Chat Room

AOL keyword: BW Talk

Transcripts of all conferences are available for downloading from the BW Online area on AOL soon after each event

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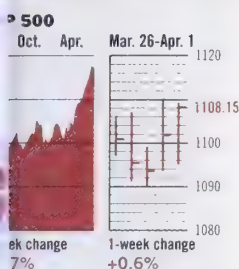
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Investment Figures of the Week

CKS



MENTARY

the record books. The quarter wound up on Mar. 11th the Dow industrials fell under 8800, up 13.1%, the S&P 500 at nearly up 13.5%. Driven by the tech stocks, the NASDAQ composite logged 16.9% to a new high. All told, the first quarter was the best since 1987's. The rally continued into the new quarter as the S&P and the NASDAQ went on to make new highs on Apr. 1. The Dow added 69 points that day, too, but is still 40 shy of a new

U.S. MARKETS

	Latest	% change	
		Week	Year
Dow Jones Industrials	8868.3	-0.1	36.1
NASDAQ Combined Composite	1847.7	1.3	53.8
S&P MidCap 400	372.5	1.1	49.5
S&P SmallCap 600	202.9	1.9	50.1
S&P SuperComposite 1500	237.7	0.7	48.0

SECTORS

	Latest	% change	
		Week	Year
Bloomberg Information Age	340.7	0.6	52.2
S&P Financials	132.9	-0.7	57.6
S&P Utilities	246.2	-0.7	30.5
PSE Technology	351.9	1.9	47.8

FOREIGN MARKETS

	Latest	% change	
		Week	Year
London (FT-SE 100)	6017.6	0.8	42.0
Frankfurt (DAX)	5154.2	1.1	56.1
Tokyo (NIKKEI 225)	16,241.7	-2.5	-10.0
Hong Kong (Hang Seng)	11,331.4	-4.1	-6.6
Toronto (TSE 300)	7527.9	-0.7	28.7
Mexico City (IPC)	4999.1	0.0	34.5

FUNDAMENTALS

	Latest	Week ago	Year ago
S&P 500 Dividend Yield	1.41 %	1.36 %	1.94 %
S&P 500 P/E Ratio (Last 12 mos.)	27.8	27.7	19.9
S&P 500 P/E Ratio (Next 12 mos.)*	21.5	21.9	15.9
First Call Earnings Revision*	-3.43 %	-3.48 %	NA

TECHNICAL INDICATORS

	Latest	Week ago	Reading
S&P 500 200-day average	963.0	957.4	Positive
Stocks above 200-day average	66.0 %	67.0 %	Neutral
Options: Put/call ratio	0.53	0.58	Negative
Insiders: Vickers Sell/buy ratio	2.62	2.52	Negative

Data: Bloomberg Financial Markets; *First Call Corp.

BEST-PERFORMING GROUPS

	Latest	Last month %	Last 12 months %
Soft Drinks	18.5	Homebuilding	109.4
Pollution Control	18.0	Broadcasting	105.3
Office Equip. & Supplies	17.8	Communications Equip.	97.0
Restaurants	13.7	Specialty Appar. Retailers	94.3
Invest. Banking/Brkrge.	13.1	Personal Loans	93.0

WORST-PERFORMING GROUPS

	Latest	Last month %	Last 12 months %
Tobacco	-8.1	Metals	-29.6
Semiconductors	-5.2	Shoes	-27.9
Toys	-4.1	Gold Mining	-21.5
Computer Systems	-3.3	Photography/Imaging	-6.6
Manufactured Housing	-3.1	Engineering & Constr.	-5.7

BLOOMBERG MONEY FLOW ANALYSIS

Rebound ahead? Stocks with most significant buying on price weakness

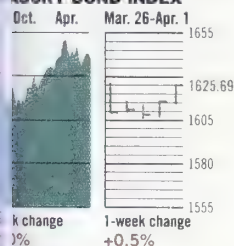
	Price	1-month change
Lockheed Martin	112 1/2	-3
Micron Technology	29 1/16	-5 9/16
General Motors	67 3/4	-3 1/8
Chevron	80 9/16	-2 1/4
Compaq Computer	25 7/8	-5 1/4
W.R. Grace	83 11/16	-1/16

Decline ahead? Stocks with most significant selling on price strength

	Price	1-month change
Microsoft	89 1/2	6 3/16
WorldCom	43 1/16	4 9/16
Pfizer	99 11/16	11 7/8
Cisco Systems	68 3/8	3 1/8
PeopleSoft	52 5/8	8 7/16
Costco	53 3/8	3 3/8

REST RATES

ASURY BOND INDEX



Bloomberg Financial Markets

KEY RATES

	Latest	Week	Year
		ago	ago
MONEY MARKET FUNDS	5.11	5.11	5.01
90-DAY TREASURY BILLS	5.10	5.18	5.30
6-MONTH BANK CDS	5.05	5.07	5.13
1-YEAR TREASURY BILLS	5.35	5.40	5.98
10-YEAR TREASURY NOTES	5.58	5.64	6.88
30-YEAR TREASURY BONDS	5.88	5.94	7.08
LONG-TERM AA INDUSTRIALS	6.45	6.51	7.56
LONG-TERM BBB INDUSTRIALS	6.93	6.98	7.94
LONG-TERM AA TELEPHONES	6.74	6.79	7.77

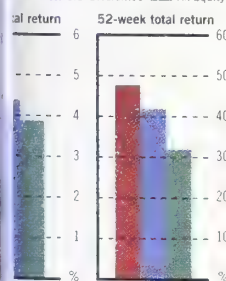
BLOOMBERG MUNI YIELD EQUIVALENTS

Taxable equivalent yields on AAA-rated, tax-exempt municipal bonds, assuming a 31% federal tax rate.

	10-yr. bond	Latest	30-yr. bond	Latest
	Latest	week	Latest	week
GENERAL OBLIGATIONS	4.45%	4.43%	5.05%	5.03%
PERCENT OF TREASURIES	78.63	78.54	85.02	84.64
TAXABLE EQUIVALENT	6.45	6.42	7.32	7.29
INSURED REVENUE BONDS	4.59	4.57	5.24	5.21
PERCENT OF TREASURIES	81.10	81.02	88.22	87.67
TAXABLE EQUIVALENT	6.65	6.62	7.59	7.55

AL FUNDS

10** U.S. Diversified All Equity



Morningstar, Inc.

EQUITY FUNDS

Leaders		Laggards	
Four-week total return	%	Four-week total return	%
Amerindo Technology D	16.3	DFA Japanese Small Co.	-12.3
Weitz Hickory	13.5	Capstone New Zealand	-9.6
First Eagle International Y	12.2	Fidelity Japan Small Co.	-9.4
Calvert New Africa A	11.8	Japan	-8.9
Smith Barney Telecom. Inc.	11.4	Barr Rosenberg Japan Instl.	-7.8
Leaders		Laggards	
52-week total return	%	52-week total return	%
Delaware Aggressive Gr. A	103.1	U.S. Global Investors Gold	-55.2
Munder Micro-Cap Equity Y	88.1	Midas	-51.9
FMI Focus	85.1	Merrill Emerging Tigers B	-47.2
Fidelity Select Brokerage	85.1	Bull & Bear Gold Investors	-47.0
MAS Mid Cap Growth Instl.	77.3	Morgan Stan. Asian Grth. C	-46.0

EQUITY FUND CATEGORIES

Leaders		Laggards	
Four-week total return	%	Four-week total return	%
Communications	8.1	Japan	-5.9
Utilities	6.3	Diversified Pacific/Asia	-3.1
Precious Metals	6.2	Pacific/Asia ex-Japan	-0.2
Europe	5.9	Natural Resources	1.7
Small-cap Growth	5.1	Real Estate	2.4
Leaders		Laggards	
52-week total return	%	52-week total return	%
Communications	61.5	Precious Metals	-32.3
Financial	56.2	Pacific/Asia ex-Japan	-30.4
Large-cap Growth	47.3	Diversified Pacific/Asia	-22.7
Small-cap Blend	44.1	Japan	-10.2
Unaligned	42.9	Diversified Emerging Mkts.	-7.4

as of market close Wednesday, Apr. 1, 1998, unless otherwise indicated. Industry groups P 500 companies only. Fundamentals, technical indicators, Bloomberg money flow analy-

sis, and mutual fund returns are as of Mar. 31. For a more detailed explanation, write to us or E-mail figures@businessweek.com. NA=Not available **Vanguard Index 500 Fund

TOKYO IS COURTING DISASTER

A crisis in Japanese capitalism is unfolding. In the months ahead, the yen could weaken to 150 to the dollar from 133 and the Nikkei could plummet to 12,000, less than one third of its 1989 peak. Unless steps are taken soon to reverse course and reboot the Japanese economy, Asia's recovery will be jeopardized—and the U.S. and Europe could be hit with the biggest deflationary wave since the Depression.

A "sell Japan" mentality is already taking hold among the Japanese. Here are the facts: Profits, wages, and prices are falling fast. Industrial production dropped 3.3% in February from the month before, and the International Trade & Industry Ministry forecasts an additional 5% drop in March and April. These are huge declines, beyond what is seen in typical recessions. Auto, housing, and retail sales are all in sharp decline. A toxic combination of misguided government economic policy, political paralysis, and financial deregulation is setting the stage for massive capital flight.

The latest government pump-priming effort, like the dozen or so before it, is unlikely to work. Why? Only half of the \$127 billion stimulus package is "pure water," or new money, and most of that will go to public works, not tax cuts. Construction companies receiving the largesse are likely to kick back campaign contributions. With elections looming, the Liberal Democratic Party wants to target spending in election districts to support its candidates. A massive tax cut that could restore consumer confidence is not to be (page 28).

The Nikkei appears to agree. Stocks failed to rally when the program was announced, and the index closed at 16,527. Banks and insurance companies were expecting the Nikkei to end its fiscal year in March at 18,000—last year's close. Now, they could be hit by stock valuation losses and forced to cut lending, exacerbating Japan's already severe credit crunch.

It's a dismal economic scenario—and it gets worse. Monetary policy has failed even though interest rates are down to 1% to 1.5%. Terrified of losing their jobs for the first time in

their lives, people are curbing consumption and saving mad. Trouble is, with rates so low, they can't get a decent rate of return. And the stock market is no alternative. What are Japanese savers to go?

Enter the Big Bang. Financial deregulation begins on April 1. By deregulating securities markets and cutting broker commissions, opening banking and insurance, and removing currency controls for retail accounts, Tokyo hopes to revitalize the economy. It may do so over time, but financial deregulation within a stagnant economy could first cause a *leakage* of money out of Japan as citizens, seeking higher returns, invest abroad for the first time. "Sell Japan" could become a reality as people buy dollars and dump the Nikkei for the dollar.

Japan is stuck. Its old policies, once successful, are failing. In the past, devaluing the yen always boosted growth through exports. Today a weak yen is self-destructive. Some 40% of Japanese exports go to Asia, and the more Japan devalues the more it hurts Asian growth and Japanese exports. Devaluation undermines competing Asian chips, cars, and steel on world markets and raises prices on imports to Japan. A weak Asia means lower profits for Corporate Japan.

Massive tax cuts and a stronger yen could restore consumer buying power and confidence and lift Japan out of its seven-year stagnation. The economy was growing last year before Tokyo slammed it by raising VAT taxes 2%. But policymakers would have to shift mental gears. Japan is no longer run as a pension state, with policy directed at providing retirement. Growth is not the goal, even though it is the solution to the pension problem. A few corporations compete globally while the domestic economy stagnates. Investments made overseas in the glory years of the 1980s provide income. Japan is in decline. The economic dynamism that was the hallmark of postwar Japan is shifting to China.

This ominous script can be averted. But given the nature of Tokyo's policymakers, it may take a crisis to save Japan.

THE NEW PARTY OF BIG SPENDERS

Is the GOP about to become the party of pork and campaign sleaze? Are big spenders now Republican congressional legislators? Is the party of term-limiters now the party of status-quo fat cats? Good questions—and if the leadership of the Republican Party doesn't have good answers, they are seriously misreading the American public.

The gargantuan \$217 billion highway bill is a throwback to the days before budget discipline. Using nearly 1,600 individual projects as bait, Transportation Committee Chairman Bud Shuster (R-Pa.) masterminded a log-rolling jamboree and called it legislation (page 41). It exceeds the spending limitations on the current budget by \$30 billion and provides

such goodies as a 54¢-a-gallon ethanol subsidy (totally unnecessary with gasoline prices so low). There was a time, not long ago when Republicans stood for fiscal austerity.

There was also a time when they backed term limits for a better government. But that was before they took power in Congress. The trashing of campaign-finance reform was not enough. But the unabashed glee GOP leaders took in lambasting an honorable man, Republican reform leader Christopher Shays of Connecticut, risks a serious split within the party. Blasting Bill Clinton and the Democrats for campaign-finance violations while blocking efforts at reform reeks of hypocrisy. What on earth is House Speaker Newt Gingrich thinking?

BusinessWeek

20, 1998 A PUBLICATION OF THE MCGRAW-HILL COMPANIES \$3.95

WHAT TO DO ABOUT MICROSOFT

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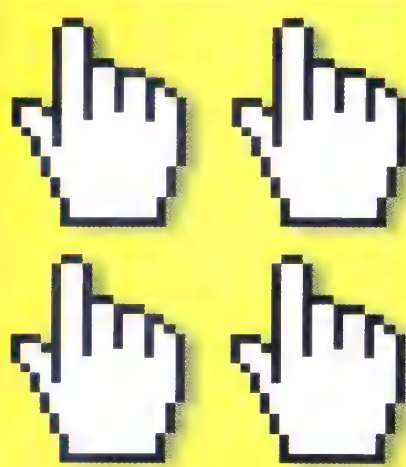
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Break It Up



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Readers:
Tell us what you think PAGE 126



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WHAT TO DO ABOUT MICROSOFT
We offer three broad options for dealing with the 800-lb. gorilla of the computer business—and the economy
page 112

BusinessWeek

APRIL 20, 1998

Cover Story

112 WHAT TO DO ABOUT MICROSOFT

The pervasiveness of Microsoft in the digital world raises profound questions: Should one company wield such might? And what, if anything, should the government do about it? Here are three broad options:

SCENARIO 1: LEAVE GATES ALONE

The market will ultimately discipline Microsoft, as it did IBM

SCENARIO 2: SLOW THE GIANT

Using "surgical strikes," special rules would be applied to Microsoft

SCENARIO 3: BREAK MICROSOFT IN TWO

Oddly, the strongest government action may in fact be the free-market answer

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Up Front

EDITED BY ROBERT McNATT & LARRY LIGHT

SUPERINVESTORS

A PRINCE IN PLANET HOLLYWOOD'S ORBIT

FRESH OFF A BIG PAYDAY—when the proposed Travelers-Citicorp merger ballooned his 1991 investment in Citicorp by \$1.5 billion—Prince Alwaleed bin Talal is scouting out a smaller investment. The Prince has confirmed that he is talking with Singapore developer Ong Beng Seng about buying Ong's stake in Planet Hollywood International's master franchise in Asia, which includes eateries in

Australia, Hong Kong, Indonesia, and Thailand. The transaction may be chump change for Alwaleed, whose current franchises and 4% equity stake in Planet Hollywood may total \$140 million. But buying Ong's Asian franchises could make life easier for Ong. Stung by the Asian financial crisis, the developer is cashing in his holdings, says a business associate.

Ong did not **ALWALEED BIN TALAL**



comment. But the public company he controls, Hotel Properties Ltd., has already sold several properties, including a stake in a planned Planet Hollywood hotel in New York. Ong personally owns 23.6% of the chain's shares, but Alwaleed isn't interested in that stake.

Aside from Citicorp, he never buys more than 4.9% of U.S. public companies.

Planet Hollywood said it hadn't discussed buying Ong's shares, though the company is still eyeing the Asian franchise.

Gail DeGeorge



WANTED: New image

MAKEOVERS

GATEWAY 2000: NO LONG FOR THE FARM

HERE'S AN IMAGE TO BEHOLD: Ted Waitt, the youthful CEO of Gateway 2000, running bare-chested and toting a surfboard on a California beach. It would be pretty routine for Waitt, who wasn't such a boogier in South Dakota and has based the company in New Sioux City. But Gateway's top executives will soon start working in San Diego. So a cow in the pasture—its folksy marketing image—will soon play a lesser role, say some analysts.

The administrative offices will be just down the road from the new sales unit in Irvine that caters to corporate, government, and educational users. Those customers, 30% of the PC maker's market, aren't interested in cow "The 'in your face... space cow' will be downplayed," predicts Sean Kaldor, an analyst at International Data Corp. "They want to see about solid, reliable service."

Now, Gateway could be out the same message as the Great Plains, too. But new offices will allow Waitt to commute from his \$140,000 home in suburban San Diego. So will corporate headquarters eventually follow the CEO? Waitt's not saying. But the company says it's a lot easier to attract workers to California than the Dakotas. Roger Crandall

CAR TALK

AN SUV MAY STOP SATURN'S ECLIPSE

GENERAL MOTORS' STRUGGLING Saturn Div. is ready to barge into one of the industry's hottest segments by developing its long-rumored small sport-utility vehicle. Mark Hogan, vice-president in charge of small-car development at GM, confirmed on Apr. 8 that "it's in the pipeline."

Saturn needs a winner.

Sales have declined 15% so far this model year in a brutal market for small cars. Analysts have blamed Saturn's slide on a lack of new products: The division has sold the same basic little car since it started in 1990.

GM has said that a midsize Saturn sedan is coming next year, but the company hadn't confirmed rumors of a

sport-utility vehicle or minivan until now.

Hogan says the new sport-utility would take on the wildly popular Honda CR-V and Toyota RAV4. "The mini-utility market is growing at a 20% annual clip, with most of that going to the CR-V and RAV4," he says.

However, the wheels of change move ever so slowly at General Motors, and analysts don't expect to see a Saturn SUV until 2001 at the earliest. Keith Naughton

THE LIST IF TICKETS REFLECTED THE COST OF MOVIES

At a recent movie industry confab, Seagram CEO Edgar Bronfman Jr., also head of Universal Studios, griped that his industry charges the same price for tickets, regardless of a movie's cost. So given an average



LOST IN SPACE: Is the price right?

ticket price of \$5 and production cost of \$52 million, we did some cost-based pricing. Sure, *Titanic* is a smash, but would you pay almost \$20? At least you could see *The Full Monty* for barely nothing.

	PRODUCTION COST (\$ MILLIONS)	TICKET PRICE
TITANIC	\$200	\$19.20
GODZILLA	125	12.02
TOMORROW NEVER DIES	100	9.61
LOST IN SPACE	70	6.73
PRIMARY COLORS	65	6.25

	PRODUCTION COST (\$ MILLIONS)	TICKET PRICE
AS GOOD AS IT GETS	52	5.00
THE MAN IN THE IRON MASK	45	4.32
L.A. CONFIDENTIAL	32	3.07
GOOD WILL HUNTING	16	1.53
THE FULL MONTY	3	0.29

DATA: EXHIBITOR RELATIONS CO., BUSINESS WEEK

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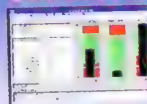
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Up Front

RETAIL TALES

BLOCKBUSTER'S EARLY-BIRD SPECIAL

BLOCKBUSTER VIDEO SAYS it is cashing in on the obvious: Pay people to return their rentals early, and they'll rent more videos.

In December, the company unveiled an "early-bird" incentive plan to boost rentals of new releases. Customers pay an average of \$2.76 for a copy of, say, *The Full Monty*, for two evenings. But those who bring the flick back before 8 p.m. on the second evening get \$1 off a new film rented the same evening—plus free popcorn.

That cuts the cost of renting two videos by about 15%. It also keeps more of the releases most in demand available, easing a perennial prob-



DISCOUNT DEAL

lem for Blockbuster, which continues to charge a late fee per video of \$2.99 or less per day if returned after midnight of the second evening. The

company says the plan covers the cost of the bonus for the 14% of customers who already return videos on time, and is profitable.

How much more profitable than the old policy? Blockbuster won't say, but is pleased. "We've seen a significant increase in the number of customers who rent on return," says marketing senior

vice-president George Williams. Which shows that you can catch more couch potatoes with honey than with vinegar.

Stephanie Anderson Forest

FUND FRONT

WHERE TO KEEP YOUR NEST EGG WARM

LOOKING FOR A PLACE TO PUT 401(k) cash? Index funds are still tough to beat. Although 6 of the 10 largest mutual funds owned by 401(k) investors equaled or beat the

Standard & Poor's 500-stock index in the first quarter, only half of those—Putnam Voyager (A), Fidelity Magellan, and 20th Century Ultra—were actively managed.

The glimmer of good news for those who haven't owned index funds—the vast majority of 401(k) investors—is that actively managed funds are faring better. William Dougherty, president of Kanon, Bloch, Carre, a Boston 401(k) consultant, says that of 500 actively managed funds he tracks that are widely held by 401(k) investors, 30% outperformed the market in the first quarter. That's up sharply from the 10% that beat the market last year and the 3% that beat it over three years, he says.

But managed funds have one edge, he says. In the inevitable market drop, they shouldn't fall as far as their indexed cousins. *Geoffrey Smith*

10 Most Widely Held Funds by 401(k) Investors

NAME	Q1 RETURN
20TH CENTURY ULTRA	15.9%
PUTNAM VOYAGER (A)	14.6
FIDELITY MAGELLAN	14.2
VANGUARD INST. INDEX 500	14.0
FIDELITY SPARTAN EQ. INDEX	13.9
VANGUARD INDEX 500	13.9
S&P 500 (WITH DIVIDENDS)	13.9
VANGUARD WINDSOR	12.8
FIDELITY GROWTH & INCOME	12.7
FIDELITY CONTRAFUND	12.3
FIDELITY EQUITY INCOME	11.4

DATA: KANON, BLOCH, CARRE, MORNINGSTAR

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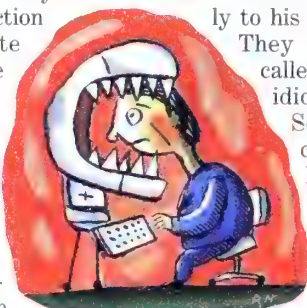
DON'T YOU DARE DIS DELL

SURE, IT WAS JUST A BAD knock on a stock. But the stock was highflier Dell Computer, and analyst Craig Kaufman wasn't ready for the vituperative reaction he got in late March after he told investors to bail out.

Kaufman's "sell" appeared on the Web site of Kaufman Brothers, a small technology-focused broker in New York. It said the PC market is so competitive, Dell's growth has to slow. It also called the stock, up some 60% this year, overvalued. Although other analysts recently downgraded Dell, none told

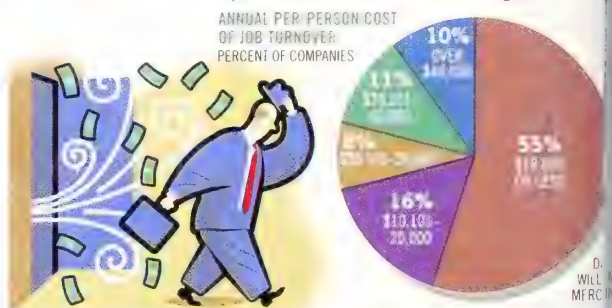
investors to sell, a rare move. Dell merely asked for a copy of the report, says Kaufman. But almost 100 individual investors reacted furiously to his online analysis.

They flamed. They called him lazy, idiot, pathetic. Some even accused him of holding a sex position in the stock, which he denies. They guess there's a reason so many of people don't go out on a limb," says a stunned Kaufman. "But we are trying to build credibility with investors." It seems that some of them prefer good news to honest advice.



THE BIG PICTURE

JOB-TURNOVER TAB How much does it cost when an employee leaves? Factor in lost productivity from a vacancy, search fees, management time used to interview, and training costs for a new hire, and here's what 206 companies say

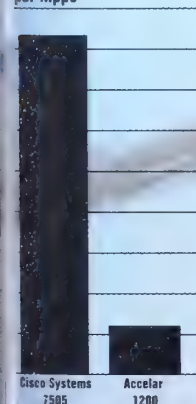


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THOSE DWINDLING EARNINGS— AS STOCK PRICES SOAR

Your statistics in "The best performers" (Cover Story, Mar. 30) were enlightening. But for many companies, there is no relationship between earnings and market return. Even companies with solid earnings growth have their market values increase twice as fast as profitability.

I guess, in the new economy, the relationship between market price and earnings is irrelevant; if earnings decline, it is an "extraordinary event." With stock prices going up so quickly, everything is a growth stock, as the average dividend yield dwindles. And I thought Japan was part of the new economy. Maybe it is—just farther ahead of us.

Robert M. Singer
Hamden, Conn.

PRIMERICA: CARING FOR MIDDLE-INCOME FAMILIES

Thank you for spotlighting our CEO, Joseph J. Plumeri II, in "The apostle of life insurance" (People, Mar. 30). Primerica Financial Services owes much of its current momentum to the enthusiasm Joe brings to every meeting and company event. But PFS is also a cadre of men and women like myself who are equally as passionate about changing the quality of life of middle-income families across North America. Whether we work full- or part-time is immaterial.

We are putting families on the road to financial independence by providing the right value-added services and products, of which income protection is just one. Our loan and debt-elimination programs are saving families hundreds of thousands of dollars in unnecessary interest payments. Our auto and homeowner's policies save families thousands of dollars in excessive premiums.

I take offense at the evaluation of our Financial Needs Analysis as "nothing special." The FNA is a unique tool designed to give a family a customized and confidential assessment of their financial

CORRECTIONS & CLARIFICATIONS

In the tables accompanying "The BUSINESS WEEK 50" (Cover Story, Mar. 30), the correct market value for Cendant Corp. is \$31.4 billion. In the Alphabetical List of Companies that would make its market value rank 6.

"Ratings services rush the Net" (In Business This Week, Apr. 6) should have stated that Nielsen Research Media is a unit of Cognizant Corp.

The photo accompanying "The earth shifting under heavy equipment" (News Analysis & Commentary, Apr. 6) shows Caterpillar Inc. machinery at a Tacoma (Wash.) dock. New and used machines were on the dock that day, and Caterpillar says those pictured were not gray-market goods returning from Asia, but new machines arriving from offshore Caterpillar plants for sale in the U.S.

situation today and where they'll be at retirement. More than this, it identifies exactly what changes a family needs to make to become debt-free, financially independent, and capable of enjoying the kind of retirement they desire.

Max H. H.
Walnut, Calif.

ARE WALL STREET MIDDLEMEN DOOMED, LIKE BRAKEMEN?

"Market of the future? Don't hold your breath" (News: Analysis & Commentary, Mar. 30), about the threats market makers and other Wall Street middlemen, made me think of how technology has made other jobs obsolete, such as the brakemen on railroad tracks. I presume that none of these Wall Streeters would condemn trade unions for requiring employers to keep people in obsolete jobs. To condemn them would be logically inconsistent, yet to do so would betray their "free-market" ideology. The markets should either yield to the most efficient solution or admit that they don't support a free-

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get economy. Otherwise, these people will be the brakemen of the 21st century, perhaps in more ways than one.

Victor Riley
Shoreview, Minn.

LE TV: 'CONSUMERS ARE UP AND WANT A CHOICE'

People wholeheartedly agree with "Tele-Let the free-for-all begin" (Editorial, Mar. 30) that all communications markets should be opened up to competition. In fact, our cable-TV operations prove competition works for consumers. Ameritech has not ignored cable customers' pleas for help. We have won franchises to compete for more than 100 homes in 70 Midwestern cities and towns. We now serve more than 100,000 customers, placing Ameritech among the top 50 cable companies in the country in less than two years of operation. Those customers have chosen Ameritech service over an incumbent, formerly monopoly, provider.

As you show, cable rates continue to skyrocket where incumbents retain their monopoly. But unlike direct broadcast satellite, where we compete, rates have stabilized or even dropped. We're in the marketplace to stay. Why? Because consumers are fed up and want a choice.

Deb Lenhart
President
Ameritech New Media
Chicago

NT ONE TREE EVERY AMERICAN

We should applaud Toyota for environmental innovation ("Only God and Toyota can make a tree," Environment, Mar. 30). Toyota plans to line Japan's highways with trees to reduce carbon-dioxide levels. Admittedly, urban tree planting and reforestation represent only a partial solution. Experts differ on the number of trees needed to offset the carbon emissions from a single car.

Nevertheless, as we continue to seek environmentally friendly automotive technologies, there is much we can do. As a retired city planner, I would like to see the automotive, petroleum, and related industries follow Toyota's lead. These industries should dedicate themselves to a 10-year goal of planting one tree for every American, first on urban streets and arterial highways. A new crop of trees could renew these corridors as green parkways and natural carbon-dioxide storage centers. Who would actually handle the greening of America? How about giving the task to inner-city youths.

Willard Cooper
Cherry Hill, N.J.

HOW DRUG ADS HELP THE PATIENT

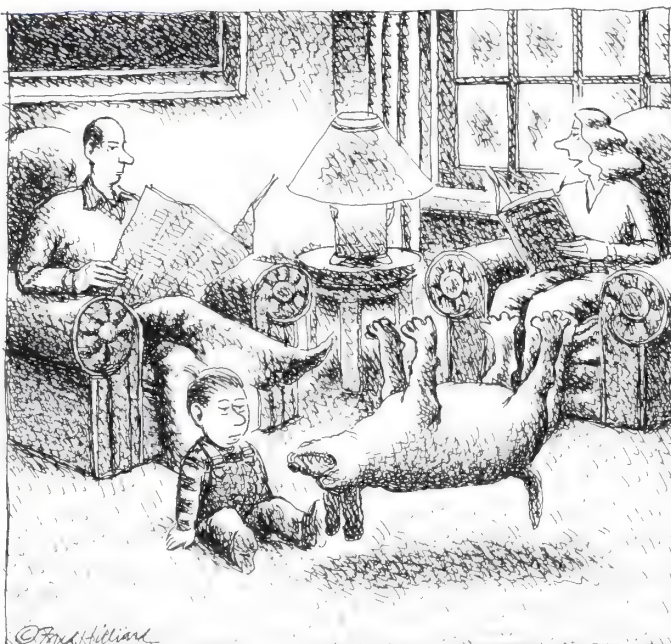
"Are drug ads a cure-all?" (Marketing, Mar. 30) missed a key part of the story—the patients. The advent of consumer drug advertising is symptomatic of bigger societal issues: the emergence of managed care, the coming of the Information Age, and a collectively empowered populace.

Advertising drugs often provides much needed data, hope, and reassur-

ance to consumers seeking information on diseases and therapy. In addition, since prescription drugs can be obtained only from a physician, the belief is that the advertising can actually encourage a dialogue or better partnership between doctor and patient.

We have seen research indicating that doctors respond positively to consumer brand requests. Often, they feel it promotes better drug compliance and helps patients feel more involved in their therapy, which in turn increases positive

WillTales

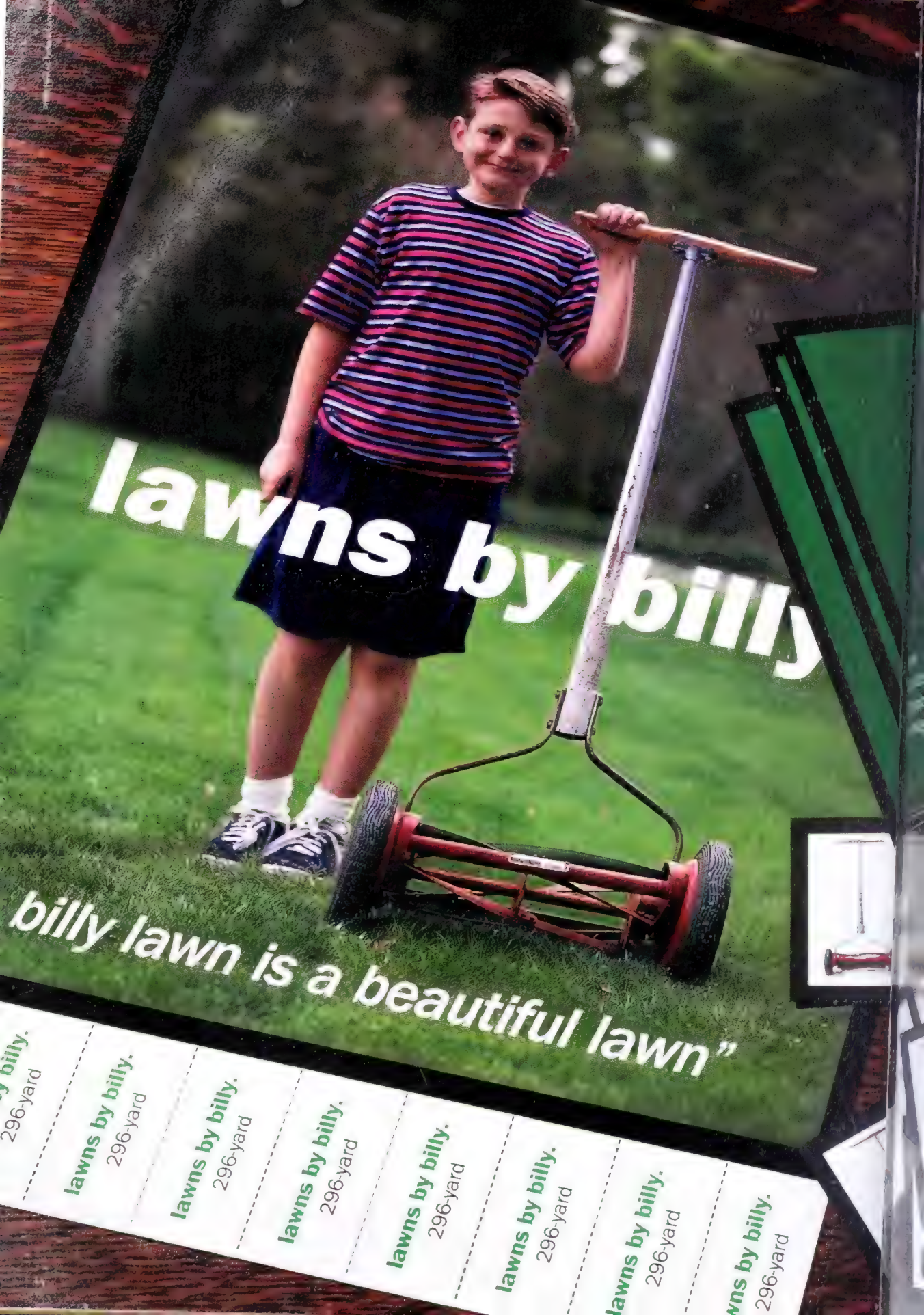


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Readers Report

outcomes. Finally, for a prescriber, a patient's request for a brand may be the tie-breaker if there are parity products available.

Deborah Dick-Rath
Senior Vice-President
Quantum Group
Parsippany, N.J.

MAKE THE TOBACCO COMPANIES WEAN SMOKERS OFF NICOTINE

In "Is big tobacco's antismoking push a smokescreen?" (News: Analysis & Commentary, Mar. 30), there is discussion of increased taxes, education incentives, and more spending on health care. Doesn't anyone get it? It's the nicotine! We know the tobacco industry manipulated tobacco to increase nicotine. Now, they must be required to reverse what they have done.

Increased taxation is not the fix: It would instantly create a black market for cheaper tobacco. Prescription control is not practical and too expensive. Education will only help a little—most people know that smoking is a serious health problem. A drastic immediate reduction would be impossible to institute, what with the cries of smokers' rights and the lobbyists who would argue constitutional rights.

But there is a way: Establish a maximum nicotine level that reflects the amount in cigarettes today. Require a reduction by 5% per year until nicotine is reduced by 80% or more. The beauty of such a proposal is that smokers would not be severely impacted. The industry would have many years to rettool. It would not create an instant black market for stronger tobacco. Monitoring for compliance could be done with minimal random testing. Substantial fines could be imposed for violations.

Most important, new smokers (and there will be new ones every day) would not be so easily hooked. When they realize they should quit, they would have the ability to do so. We owe this to the children who will always try new things but don't have the wisdom or experience to avoid such a strong chemical addiction.

J. Terrell Kirsch
Thousand Oaks, Calif.

THE STATE OF THE ART IN CATARACT SURGERY

At present, more than 98% of cataract patients experience improved vision as a result of modern surgical techniques, and constant refinements continue to improve those outcomes ("A

cataract breakthrough may be on the way," Science & Technology, Mar. 23).

The Catarex system, the focus of your article, is one of several new technologies under development that have the potential of improving the cataract procedure. We will have to wait for the results of clinical trials in humans, though, before we can evaluate the safety and effectiveness of any of these new procedures.

It's a mistake to believe that Catarex or any procedure like it wouldn't require the talents of a skilled ophthalmic surgeon. Cataract surgery would continue to be an invasive micro-surgical procedure with the same risks and benefits as phacoemulsification, the procedure that is today's standard of care.

Moreover, it is not the method of cataract removal that is the key to future breakthroughs: It is the development of biomaterials that will allow for accommodating lenses. We're still many years and many hurdles away from being able to offer this kind of intraocular lens solution to our patients.

Finally, for about the same fee as the cost of a root canal, ophthalmologists perform this skill-intensive procedure. It is a small price to pay for the independence and improved quality of life that cataract surgery offers our nation's senior citizens.

Samuel Masket
American Society of Cataract
& Refractive Surgery
Los Angeles

CREDIT UNIONS DON'T DESERVE SPECIAL PRIVILEGES

"Cornered credit unions come out fighting" (Washington Outlook, Mar. 16) mentions credit unions' exemption from the Community Reinvestment Act of 1977 (CRA), a law that encourages banks to make loans in low- and moderate-income areas. Credit unions are the only federally insured depository institution with such an exemption. If they are doing such a good job in serving such areas, then they should not oppose CRA coverage.

As long as all credit unions benefit from deposit insurance and other federal subsidies enjoyed by their competitors, they should be regulated and taxed like them. Thousands of very small banks serving low- and moderate-income neighborhoods do not enjoy tax or CRA exemptions—and neither should credit unions.

Kenneth H. Thomas
Wharton School
Philadelphia

IN DEFENSE OF A RIVAL TEST FOR ALZHEIMER'S

In "No shortage of moxie at Nym" (Science & Technology, Mar. 16), you indicate that the ApoE test for Alzheimer's disease is "seriously flawed" because it can neither predict nor questionably confirm the disease.

First, the test is not meant to be used predictively but as an adjunct to physician's diagnosis. Only the PS-1 can predict Alzheimer's. No test can "unquestionably confirm" Alzheimer's. That can only be accomplished at autopsy. The ApoE test has been shown to yield only 2% to 6% false positive results in peer-reviewed studies, almost twice the level claimed by Nymox for its test.

David L. Ha
Alzheimer's Disease Product Manager
Athena Diagnostics
Worcester, MA

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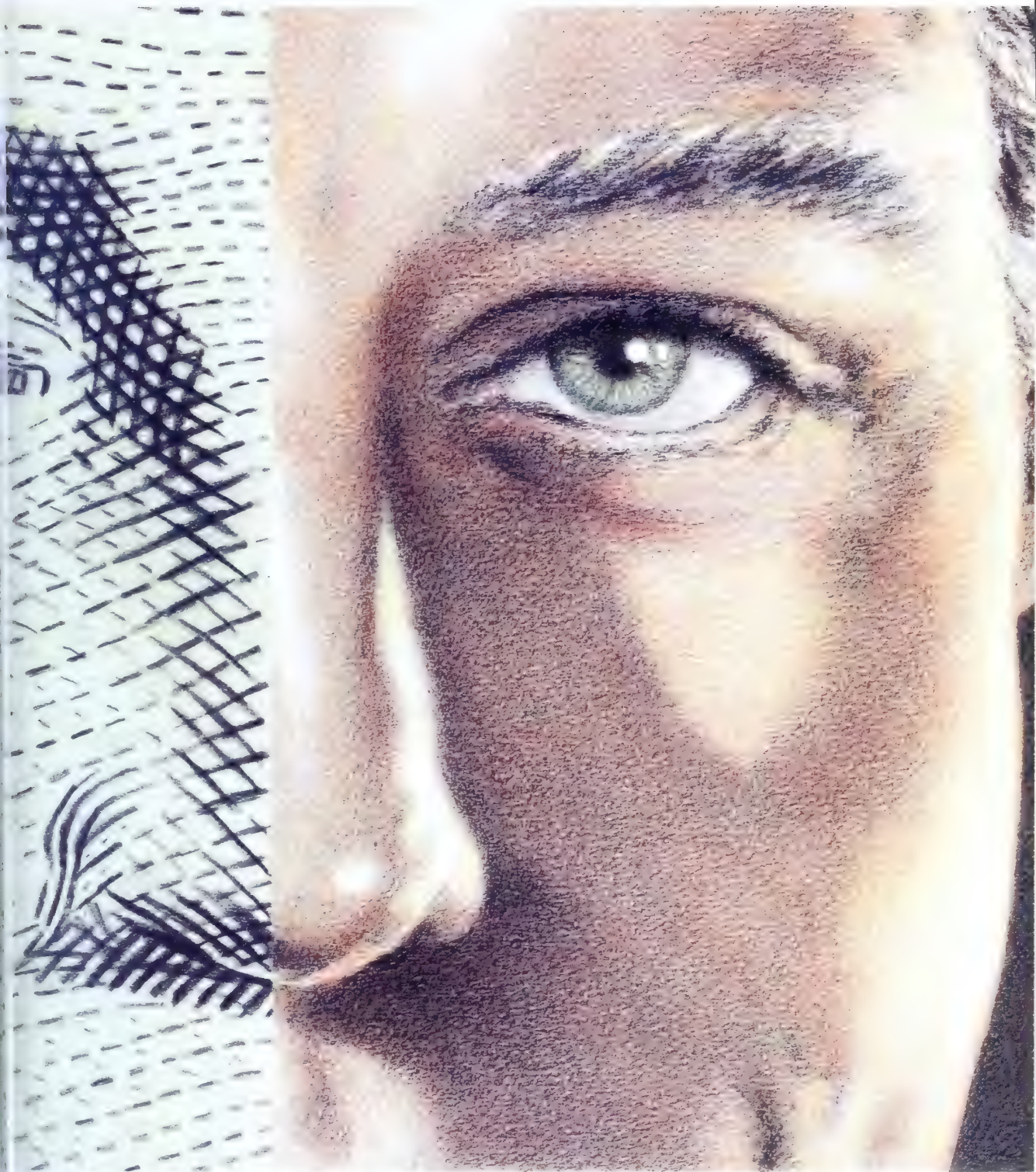
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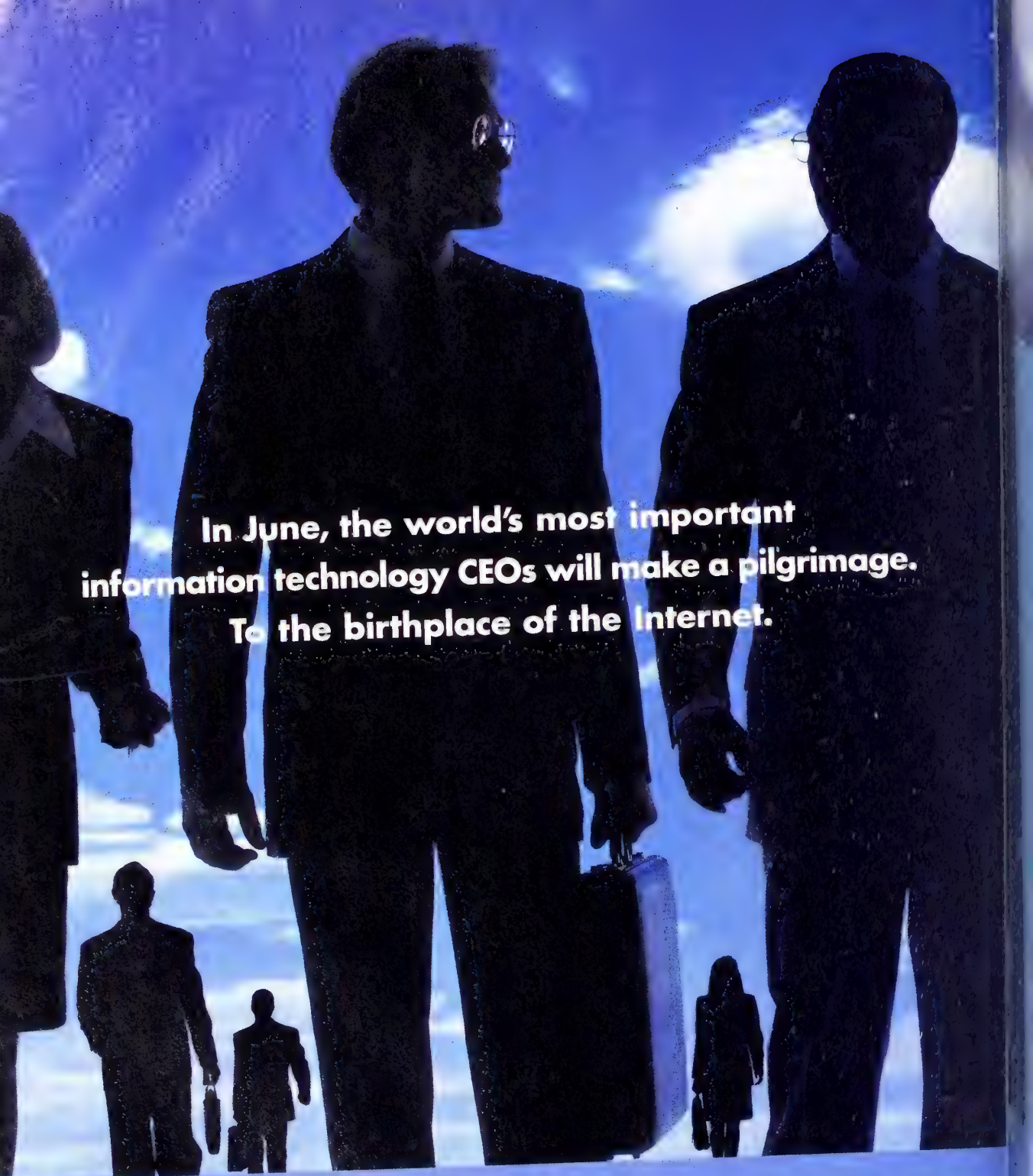
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The image features several silhouettes of people in business attire against a bright, cloudy sky. In the foreground, two large silhouettes of men in suits are prominent; the one on the left is seen in profile, and the one on the right is facing forward. Behind them, several smaller silhouettes of other professionals are visible, some carrying briefcases. The overall composition suggests a group of business leaders or executives.

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SILENCE
Unity of Knowledge
 Edward O. Wilson
 f • 332pp • \$26

AN SCIENCE MAKE SENSE OF EVERYTHING?

the summer of 1936, in the small Florida community of Paradise Beach not far from Pensacola, a 7-year-old boy sat fishing on a log, occasionally jerking a perchlike fish out of the water. When he carelessly yanked one too hard, it flew into the air, and a spine in its dorsal fin penetrated the lens of his right eye.

Pain was excruciating," he wrote years later. "But being anxious to stay outdoors... I continued fishing." Several months later, a cataract clouded the injured lens, and it was removed, leaving the boy with one good eye.

That good eye, though, turned out to be particularly acute at close range, and the boy turned it on nature. He grew to become one of the world's most distinguished biologists, responsible for many of the most influential and widely cited ideas in biology in the late 20th century.

Edward O. Wilson has spent his life studying ants, but he is best known for his efforts to link biology and human behavior. A two-time winner of the Pulitzer Prize, Wilson's writings on what he calls sociobiology have been widely cited by many researchers. In those writings, he revived the nature-nurture debate by arguing not that genes define human behavior but that they exert an important gravitational pull on it. The argument provoked fierce criticism from some who said Wilson was denying human beings in a genetic straitjacket, denying them the freedom to choose.

In his new book, *Consilience: The Unity of Knowledge*, Wilson argues for a new science of human nature, one that would help explain the social sciences, the arts, and the humanities, as well as the physical sciences.

For centuries, science has found order in a world once thought to be so mysterious as to be beyond comprehension.

Once we used myths to explain the workings of the universe and the human body. Many of those mysteries have since yielded to scientific explanation. Why, Wilson asks, should literature, music, and the arts be any different?

Wilson borrows the word "consilience" from William Whewell, a 19th-century philosopher. It means "a jumping together," and Wilson uses it to refer to the underlying links between different fields of human learning. Many such links have emerged in the natural sciences, as biologists have, for example, incorporated knowledge from physics and chemistry to help explain the workings of living cells. Wilson is now arguing for "the possibility of consilience beyond science and across the great branches of learning." The only way to establish that, he says, "is by methods developed in the natural sciences."

To make his case, Wilson takes readers on an invigorating tour through the history of ideas and some of the most exciting recent discoveries in neuroscience, complexity theory, and genetics. Wilson wanders through history, economics, sociology, religion, and literary criticism, providing illuminating thumbnail sketches of such thinkers as Darwin, Bacon, Descartes, and Einstein.

Many of the examples he discusses illustrate how scientific evidence is supplanting unscientific belief. Until the 1960s, for example, schizophrenia was thought to be a consequence of something parents did to children in the first three years of life. Now it is known that genetics plays a strong role in the development of the disease.

To take another example, Sigmund Freud, in proposing his famous Oedi-

pus complex, concluded that infant boys had a strong incestuous attraction to their mothers and that society should therefore enact "the most stringent prohibitions" to prevent such behavior. That was an intriguing explanation of incest, but it was based on Freud's interpretation of dreams—not on scientific experiment. "To put it as kindly as possible—he guessed wrong," Wilson writes. Experiments have shown, Wilson says, that humans have an intense natural aversion to incest. Many species of animals, too, avoid incest.

The most likely explanation, Wilson says, is that the aversion is a consequence of evolution. Incestuous unions produce offspring with a high chance of genetic defects, and evolution selects against that. Society therefore needs no prohibitions against incest.

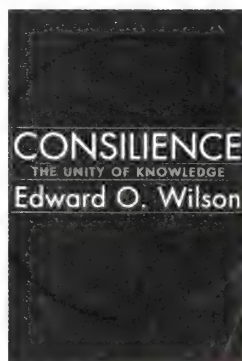
Wilson knows there are some who would say the social sciences and the humanities "are too complex to be mastered by contemporary imagination and

may lie forever beyond reach." Wilson worries about that attitude. If past generations had felt so humble before the unknown, "our comprehension of the universe would have stopped growing in the 16th century," Wilson writes. "It is the opposite conviction... that has propelled science and technology into the modern age."

Consilience is a provocative book, worth reading simply for the opportunity to spend time with one of today's great scientific minds. Nonscientists will find Wilson a congenial and approachable host. He isn't quite successful in making the case that the humanities and the arts are amenable to scientific investigation. He contends, however, that such issues as ethnic conflict, arms escalation, overpopulation, abortion, and environmental crises "cannot be solved without integrating knowledge from the natural sciences with that of the social sciences and humanities." Unifying human knowledge might be difficult or impossible, he admits. But he argues persuasively that we ought to try.

BY PAUL RAEBURN

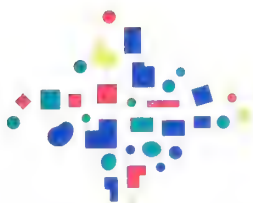
Senior editor Raeburn is the author of the forthcoming *Mars: Uncovering the Secrets of the Red Planet*.



WILSON ARGUES THAT EVEN THE ARTS ARE AMENABLE TO THE EXPERIMENTAL METHOD



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on page 166

Books

BOOK BRIEF

LESSONS LEARNED THE HARD WAY

A Personal Report

By Newt Gingrich

HarperCollins • 229pp • \$25

THE NEW NEWT

For years, Newt Gingrich has steadfastly refused to take responsibility for his shortcomings, blaming a host of others for low popularity ratings. Now, Newt has a new target: himself.

In *Lessons Learned the Hard Way*, the House Speaker and possible 2000 Presidential contender seems a changed man. The new Newt describes and explains how he was so persuaded of his revolutionary righteousness that he again and again underestimated the White House. Including the federal shutdowns of 1995, he figured Clinton would cave in; during the '97 flood-relief showdown, he ignored his lieutenants' sensible advice. "Basically," he writes, "we had only ourselves to blame."

The new Newt is also coolly analytical and more self-controlled than the undisciplined, cocky visionary who climbed to the top of the political ladder—and then was neatly toppled by his own troops just 30 months later. While the Georgian's prose doesn't soar, it offers insight into what makes this complex man tick. A rare cameo of the old Newt: the book's dense, one-sided account of his successful attempt to impeach then-House Speaker Jim Wright (D-Tex.) and of the ethics charges filed by Wright ally against Gingrich.

The heart of *Lessons Learned the Hard Way* is its account of the July 1997, attempted coup against him. As Gingrich sees it, there were no villains—except perhaps the media cultures that gleefully trashed the GOP. This report isn't likely to satisfy either conservative hard-liners, who still view the Speaker as a sellout, or liberals, who lust for more Republican bloodletting.

Overall, *Lessons Learned the Hard Way* is reminiscent of Richard M. Nixon's *Six Crises*. In both, an unpopular pol argued that he had profited from adversity, while reminding the world of his vision and relevance. Has Gingrich learned his lessons? That can't be measured by words in a book. It will be measured in the House and on the Presidential campaign trail.

BY RICHARD S. DUNHAM





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BY STEPHEN H. WILDSTROM

MICROSOFT GIVES THE MAC A HAND

New software gives Macintosh an Office suite that is the equal of Windows'

Of the many problems facing Apple Computer's Macintosh, perhaps the most serious is the reluctance of software developers to write for a system whose share of the market has fallen to 3% of sales. Even such Mac stalwarts as Adobe Systems and Quark have been shifting the weight of their graphics and publishing software to Windows.

So there is real irony in the fact that the most important new Mac software package in a long time comes from Microsoft, a company many Mac fans consider evil incarnate.

Office 98 gives the Mac a business productivity suite—software for word processing, spreadsheets, presentations, and other functions—that is at least the equal of the Windows version in performance and features. A new Office for Windows won't be out before late this year.

Historically, this update is not such an odd move. Microsoft's first important application was Excel for the Mac in 1989. Office began life as a Mac product. And Mac Office is profitable: Microsoft executives have long annoyed their Apple counterparts by pointing out that the software giant makes more money off of each Mac sold than Apple does. But Mac Office hasn't

been updated since 1994, and even Microsoft executives admit the last version was not one of the company's better efforts. Not only were its applications, especially Word, sluggish, but it drove Mac fans crazy with menus and dialog boxes that looked disconcertingly like the Windows version.

Microsoft, however, vowed to do better with Office 98—and it has. The main features are brand-new edi-

INTERNET EXPLORER: The Mac edition lacks the Windows version's tight links to the operating system, but is well-designed and probably the most stable browser for the Mac.

tions of Word, Excel for spreadsheets, and PowerPoint for presentations. This version also includes the Internet Explorer 4.0 browser and Outlook Express, an E-mail and Internet newsgroup program. There are no Mac versions of the Access database manager or the Outlook calendar and contact manager that are part of Office 97 for Windows.

The new Office costs \$450, or \$250 as an upgrade from an earlier version of Office or any of its components. A

Gold edition, for an extra \$100, adds the FrontPage Web-page editor, the Encarta Deluxe encyclopedia, and the Bookshelf reference set.

The new Office programs are reasonably zippy even on an aged Power Mac 6100 and fly on a 300-megahertz G3 computer. And they now feel like proper Mac applications, not Windows transplants. For example, Word's main menu now offers a "Font," earlier versions didn't. And the file-save dialog box offers the Macintosh choice of "save" and "don't save" instead of the Windows "yes" and "no."

POWERPOINT:

The presentation graphics program, which seemed like an afterthought in Office 4.2, gains tighter integration and greatly expanded multimedia capabilities.



OUTLOOK

EXPRESS: A full-featured E-mail program and Internet newsgroup reader, it supports the latest mail protocols and online directories.

WORD: Far faster than the predecessor, the new version has a first-rate spell checker and other proofing tools.

EXCEL: Always the strongest component of Mac Office, the latest edition of the spreadsheet gains enhanced programming capabilities.

Macs and PCs, is Visual Basic for Applications, a powerful programming language for customizing applications. Programs written for Windows Word and Excel will run on Macs, often without modification. You can read and write Windows Office 95 and 97 files and save your documents as well in the Web-ready

Hypertext Markup Language.

The Mac suite also features the excellent spell checker introduced in Windows Office 95 and the recent grammar checker from Office 97. In a feature unique to the Mac, clicking on a word while pressing the control key (an awkward maneuver that leaves me puzzled by Apple's staunch refusal to adopt a two-button mouse) brings up a list of synonyms. Click on a choice in the list, and it replaces the word in your text.

Some other Office 98 features are mixed blessings. The suite includes the Office Assistant, a cartoon character that offers you tips as you work. Windows users tend to either love or hate the Assistant; fortunately, it's easy to make it go away.

And it wouldn't be a new Office release without bugs. Under some conditions, using the "uninstall" feature may render a Mac unbootable. You can find an explanation and a fix at www.microsoft.com/macos/macosoffice. A less serious problem, also explained on the Microsoft Web site, can cause Word to quit unexpectedly when certain macro programs are run. These are relatively

minor problems in an otherwise solid release. Microsoft's commitment to the Mac, which predates the company's \$150 million investment in Apple last summer, may not be enough to make programming attractive to less well-endowed software publishers. But it's a step in the right direction. It's also a useful tool and a sign of hope for the beleaguered Mac community.



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INFORMATION, THE WAY YOU WANT IT.™

BY LAURA D'ANDREA TYSON

DON'T WORRY: CHINA ISN'T FOLLOWING IN JAPAN'S FOOTSTEPS



TWO PATHS:
While Japan remains mired in mercantilist policy, China's reforms are making it the dominant economic power in postcrisis Asia

As the U.S. trade deficit with China continues to increase, concerns mount that China will soon replace Japan as America's major trade headache. Such concerns are fed by an image of China as another Japan—a country pursuing a mercantilist development strategy based on closed markets, an undervalued currency, and a structural trade surplus.

But is China really another Japan? The evidence reveals compelling economic differences. First, although China's system poses structural barriers to foreign competition, as Japan's does, China does not enjoy a persistent current-account surplus, a defining characteristic of a mercantilist state. Rather, China's current-account balance exhibits cyclical swings, alternating between years of deficit and surplus.

Second, in contrast to Japan, China has opened its doors to foreign direct investment. In 1997, China's inflow of such investment was \$40 billion, about 40% of all such investment in the newly industrializing economies. That investment has been a major force behind China's growing international trade. By some estimates, foreign-funded companies in China account for as much as 60% of the growth in its exports over the past decade. Moreover, most of the exports originating from these companies are themselves made out of imported goods. In contrast, Japan's barriers to foreign direct investment have been a key factor behind the low import penetration of its domestic market.

BEGGAR-THY-NEIGHBOR. Third, China and Japan have responded very differently to the Asian economic crisis, which hit at a difficult time for both countries. Japan, unable to change policy, is sinking into recession, while China is embarking on a painful path of restructuring its loss-ridden banks and state-owned enterprises and is laying off millions of underemployed workers. The Chinese leadership might have been tempted to devalue the currency to grapple with the nation's economic challenges. Had they done so, they could have been justifiably tarred with the mercantilist brush. China is currently running a large trade surplus, and its reserves of dollars and yen are estimated to be three times the foreign debt of its banks. A devaluation could only be understood as a beggar-thy-neighbor tactic to export China's unemployment problem.

Instead, Zhu Rongji, China's new Premier, has announced ambitious plans to reform the banking system, to put 100,000 state-owned companies on a sound financial footing, and to cut the size of the bureaucracy by 4 million people. Chinese technocrats are rethinking the wisdom of the Japanese and Korean development models. And China has reaffirmed its commitment to foreign investors with a \$1 billion deal with Eastman Kodak Co.

Finally, unlike Japan, China has adjusted monetary and fiscal policy to shift growth away from exports toward domestic demand, especially demand for housing. China's long-run goal is to replace state ownership with private ownership of residential property. This is good news both for China's expanding middle class, who can mobilize substantial savings to achieve their housing aspirations, and for China's banks, for which mortgage lending offers a safer, more lucrative stream of revenue than do loans to state-owned companies.

THUMBS DOWN. What has Japan been doing in response to the Asian crisis? Depressing little. Japan has ignored repeated calls from the U.S. and Asian neighbors to stimulate domestic demand and has relied instead on the persistent weakness of the yen to boost exports—a striking reaffirmation of Japan's deep-seated mercantilist tradition. After helping fuel the Asian crisis, the yen weakness is now hampering prospects for recovery. Despite Japan's banks having substantial outstanding loans throughout Asia, they have failed to take the lead in organizing a global rescheduling of bad debts, leaving the task to American banks. Japan has also failed to deliver on repeated promises to dismantle systemic barriers to competition. The so-called Big Bang plan for deregulating its financial sector is moving slowly, hindered by the long-unresolved problem of nonperforming loans. No wonder Moody's Investors Service has announced a negative outlook on Japan's government debt.

China's outward-looking policy course stands in stark relief to the inward-looking timidity of Japan. China is rapidly emerging as the dominant economic power in postcrisis Asia, and its participation in the World Trade Organization, like its presence in the International Monetary Fund and the World Bank, would bolster the strength of the multilateral system.

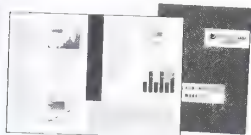
Laura D'Andrea Tyson is professor of economics and business administration at the University of California at Berkeley and was President Clinton's chief economic adviser.

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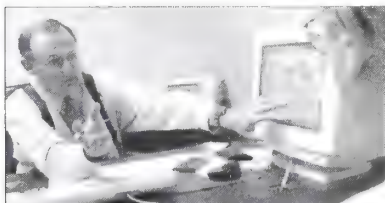
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BY GENE KORETZ

SMOKING LIKE A HOUSE AFIRE

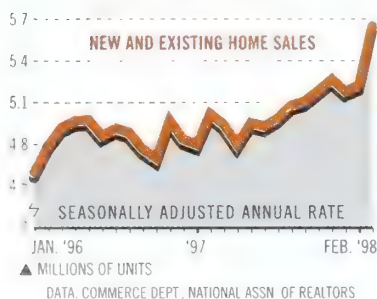
Home sales stoke the economy

Any way you slice it, observes economist Joseph LaVorgna of Deutsche Morgan Grenfell Inc., "the housing sector is really humming."

Though housing activity usually slows as an expansion ages, both starts and permits have been moving higher and hit annual rates of around 1.63 million units in February—peaks for this business cycle. And sales of new and existing homes soared to all-time highs.

Some market observers attribute the latest housing surge to the warm winter weather and still expect a slowdown. But LaVorgna is skeptical. When housing starts surged a year ago because of warm weather and then dropped back, he notes, housing permits barely budged. This year, however, permits,

IT'S A BLOCKBUSTER HOUSING MARKET



which are less sensitive to the weather than starts, are booming as well.

Meanwhile, homebuilders report that market conditions in recent months have been the strongest in several years. With inventories of unsold new homes unusually low and builders continuing to sell more homes before ground has even been broken, the market in many areas is tight as a drum.

An unusual confluence of developments is fueling the boom. Hefty job growth over the past year is lifting incomes and bolstering consumer confidence. Mortgage rates at around 7% for a 30-year loan are low, and the surging stock market helped boost household net wealth by \$3.6 trillion last year alone—enabling many consumers to decide that the time is right for the biggest investment of their lives.

The impact of all this on the economy should be considerable. Housing-related activity accounts for more than a fifth of gross domestic product, and each dollar spent on new construction or on the purchase of an existing home percolates through the economy, affecting not only sales of raw materials for construction and renovation but also purchases of furnishings, appliances, and a host of other goods and services.

"It's no accident that housing is considered a leading economic indicator," says LaVorgna. "As long as interest rates stay low, both housing and the overall economy should thrive."

WHY TAXPAYERS FILE LATE

The reasons for "Apr. 15 syndrome"

April may well be the cruelest month for the millions of American taxpayers who wrestle with their returns at the eleventh hour. To economists who assume that people are guided by economic rationality, however, it raises an intriguing question: Given their intense interest in avoiding taxes, why do so many taxpayers who are owed refunds wait until the last minute to file their returns—thus losing the earnings such refunds could provide?

In a recent study in *Economic Inquiry*, a team of researchers led by Joel Slemrod of the University of Michigan Business School analyzed tax returns filed in 1989 to throw light on what they term "Apr. 15 syndrome." They estimate that some 69 million taxpayers claiming refunds on their '88 taxes lost nearly \$1 billion in interest their money could have earned if they had filed at the end of January (today such losses could approach \$2 billion). Indeed, more than a third waited until April or later to send in their returns.

The study did find that taxpayers respond to economic incentives to some degree. People owed large refunds tend to file somewhat earlier than those owed smaller refunds, for example. And those who prepare their own returns appear to be more sensitive to such economic considerations than those who use professional preparers. But these tendencies were not particularly strong.

Perhaps predictably, the study found that more complex returns tend to be filed later than simpler returns. More puzzling is the fact that people with higher incomes, who tend to be financially savvy, are more likely to file later,

as well. Also, among those who owe taxes, the elderly have a strong tendency to file early and thus to forego the interest they might have earned if they had waited until mid-April.

In short, the major reasons for the Apr. 15 syndrome appear to lie more in the realm of psychology than economics. Many people clearly abhor the task of tax preparation and put it off as long as possible, even if they're owed a refund. Others seem to act when the growing anxiety produced by their delay finally forces them to face the music.

Whatever the reason, taxpayers don't become more economically rational over time. Looking at several years' worth of tax returns, the researchers found that procrastinators who are owed refunds tend to remain procrastinators.

WEAK PROFITS. NOT TO WORRY?

History says stocks may not slow

With the stock market up sharply last quarter in the face of scant year-to-year corporate earnings gains, fears are growing that stocks could weaken in the year ahead. But history indicates that such fears could be overblown, observes John L. Manly Jr., a financial analyst with Salomon Smith Barney.

Noting that the 13.9% return posted by the Standard & Poor's 500-stock index last quarter was the second-best in 10 years, Manly looked at the 40 best quarters from 1950 through 1997 and found that their average return was 12.3%. Moreover, the average year-to-year gain in earnings for those quarters came to less than 2%—about in line with the anemic showing last quarter is likely to post.

But the real eye-opener was the fact that the average market return in the 12-month periods following those 40 best quarters was a healthy 17.1%. In short, the historical record suggests that quarters with strong market moves in the face of weak earnings growth have more often than not been followed by years with superior stock market appreciation.

GREAT QUARTERS HERALD GREAT YEARS

TOTAL RETURN S&P 500

FIRST QUARTER 1998

13.9%

AVERAGE GAIN, 40 BEST QUARTERS 1950-1997

12.3%

AVERAGE GAIN DURING FOLLOWING YEAR

17.1%

DATA: SALOMON SMITH BARNEY

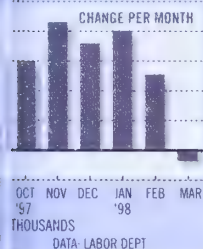
JAMES C. COOPER & KATHLEEN MADIGAN

OBS TAKE A TUMBLE, SO IS THE ECONOMY COOLING OFF?

Probably not. The dip in employment looks like a weather-related fluke

U.S. ECONOMY Most economists have been forecasting a U.S. slowdown more than a year. But despite higher real interest rates, a surging dollar, the Asian crisis, worries about inflation, or anything else analysts can think up, it hasn't happened. The reason, in large part, is strong labor markets, which are powering a consumer-led burst of domestic spending (page 42). That's why the surprisingly weak March employment report, which showed an outright drop in payrolls the first time in more than two years, deserves special attention (chart). Is it a harbinger of that long-dreaded cooling off that will purge any remaining fear that the Federal Reserve will need to raise interest rates? Or is it another false signal? The stakes are high, because Wall Street has already bought the slowdown scenario, and that forecast is built into the current prices of stocks and bonds.

PAYROLLS: EL NIÑO OR GENUINE SLOWDOWN?



But while Wall Street may yet be proved right, the March job data confirm little—except the power of El Niño. Weather and seasonal adjustment of the data were the primary influences in the swing from strong to weak hiring in the first quarter, but the trend of job growth remains strong. The only genuine slowdown appears to be in manufacturing—the result of weaker exports in the wake of falling demand. Excluding weather-sensitive industries, the trend in new service-sector jobs remains strong, and a speedup in service pay is leading the acceleration in overall wage growth.

DROP IN MARCH PAYROLLS, by 36,000 workers was totally unexpected, but a close look at the numbers shows why it occurred. First of all, an unusually warm winter caused more hiring and fewer layoffs than normal in January and February, when payrolls increased by 399,000 and 252,000, respectively. Since the government's seasonal adjustment of the data typically boosts the raw numbers in those months, January and February payrolls ended up being overstated.

When the weather turned unusually cold during the week in March that the Labor Dept. collected its data,

seasonally adjusted payrolls fell. That's because a lot of hiring that normally occurs in the month had already happened and because the cold snap restrained additional hiring.

For example, construction employment plunged by 88,000 jobs in March. Declines of that size typically occur only during recessions, but February home sales were at a record high, and construction fundamentals—from interest rates to consumer and builder confidence to soaring stock prices—haven't been this supportive in years. Restaurants posted a drop of 48,000 jobs, as eaters and drinkers decided to stay home, and employment at temporary-help firms, also subject to weather-related swings, fell 18,000.

The new weakness in manufacturing employment looks real, however (chart). After posting the strongest four-month job growth in more than a decade, factory payrolls barely rose in both February and March, and the factory workweek fell in both months. Weekly hours dropped to 41.7 in March, the lowest in more than a year, suggesting further softness in payrolls, since factories typically cut hours prior to reducing their staffs.

Overall hours worked fell steeply in March, but the increase in work time for the quarter still points to solid economic growth. Hours worked last quarter increased at an annual rate of 4.9%, even faster than the 4.5% pace in the fourth quarter. That gain suggests two things. First, despite Asia's negative impact on the trade gap and inventory growth, domestic demand continued to power overall output. And second, given the big increase in hours, productivity growth last quarter may have been poor.

CHANCES ARE VERY GOOD that hiring will rebound, perhaps strongly in April, as normal seasonal patterns take hold. Indeed, the trend in weekly claims for unemployment benefits, which has been the single best indicator of labor-market patterns in the past year, shows that the labor market remains very tight. The four-week average of claims in early April is running about 310,000, which is about where it has been since mid-February, and that level is consistent with monthly

FACTORY JOB GAINS SLOW SHARPLY



employment gains in the neighborhood of 300,000.

Hiring in the first three months of 1998 averaged a strong 205,000 per month. That pace is slower than the monthly average of 302,000 during the second half of 1997, but even at that pace—and ignoring the likelihood that April job growth will rebound—the labor markets will continue to tighten. The March jobless rate edged up to 4.7%, from February's 24-year low of 4.6%, but at job growth of more than 200,000 per month, the rate will continue to trend lower. Job growth would have to fall below about 150,000, and stay there, before the jobless rate would actually rise.

THAT MEANS WAGE GROWTH will continue to accelerate, especially in the service sector. Despite the uptick in the overall unemployment rate, joblessness in services continued to fall in March. It dipped to 4.6%, down from 4.7% and the lowest level since 1973.

It's little wonder that hourly wages in services, up 0.7% in February and 0.4% in March, are outpacing overall pay, which rose 0.6% and 0.3%, in those two months. In the first quarter, overall pay is up 4% from a year ago, while service wages have risen 4.3%, led by the finance sector (chart). Both rates are the fastest since 1990, and with inflation so low, real wages are rising at the fastest yearly clip since the early 1970s.

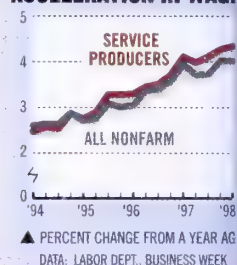
That surge in buying power is the key reason why domestic demand is so strong. March data on con-

sumer spending may also be affected by the same weather influences evident in the job data, but the underlying fundamentals have not changed. Indeed, March sales of U.S. and foreign cars and light trucks stood at a healthy annual rate of 15.1 million, a shade better than February's 15 million. Still, retailers will likely be hurt by weather effects and a late Easter.

Moreover, the gains in real earnings are helping households to unload some of their debt. Consumer installment debt, which rose \$7 billion in February, has been growing more slowly for about a year and a half, as banks have become more cautious and as households pay down some of their debt. And amid falling interest rates, consumers are swapping high-cost installment debt for cheaper home-equity loans.

Right now, as for the past year, strong labor market and vigorous demand are feeding each other. Unless something happens to break that virtuous cycle, the U.S. economy will continue to power ahead. So if you're looking for an economic slowdown, don't read too much into the March job data. Pay attention to domestic demand. When that slows, so will output, jobs and overall growth.

SERVICES LEAD THE ACCELERATION IN WAGE GROWTH



BRITAIN

A FIGHT TO STOP SERVICES FROM STOKING INFLATION

For months, the dichotomy between the unyielding strength in services and construction and the growing weakness in manufacturing has stymied economists and policymakers concerned about the inflation outlook. Now, data are starting to suggest that a broader slowdown is developing. But the crucial question remains: Is the economy slowing enough to quell rising inflation pressures?

First off, slower growth seems inevitable, if only because of current policy. Going into its Apr. 8-9 meeting, the Bank of England's Monetary Policy Committee (MPC) had lifted the base rate by 1½ points in 1½ years, to 7½%. The

MPC says growth must fall below its long-term trend of about 2.5% to assure that price pressures subside. Also, fiscal policy is still a drag—though the 1998-99 budget lessens the weight—and new tax

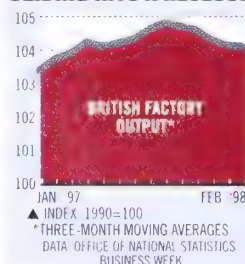
hikes are now hitting consumers. Plus, the trade-weighted pound has surged some 30% in the past year and a half, recently reaching a nine-year high vs. the German mark. That spike partly reflects concerns over Europe's single currency, the euro.

Sterling's strength has hampered manufacturers who export, putting the factory sector on the brink of recession (chart). Manufacturing output fell in the fourth quarter, and unexpected weakness

in January and February may yield a first-quarter decline. The latest survey of purchasing managers suggests continued strength in services, but domestic demand may be cooling. Official data on retail sales through February show a slower pace of buying vs. the fourth quarter, and the Confederation of British Industry reported a "marked" weakness in March retail sales.

The problem is that both wage and price pressure, while absent in manufacturing, is already visible in services. Underlying inflation—less mortgage costs—has been above the MPC's 2.5% target for two years, even given sterling's surge. Some on the MPC are worried that unless the economy slows considerably, the overvalued pound's eventual decline will only add to inflationary pressures.

MANUFACTURING MAY BE SLIDING INTO A RECESSION





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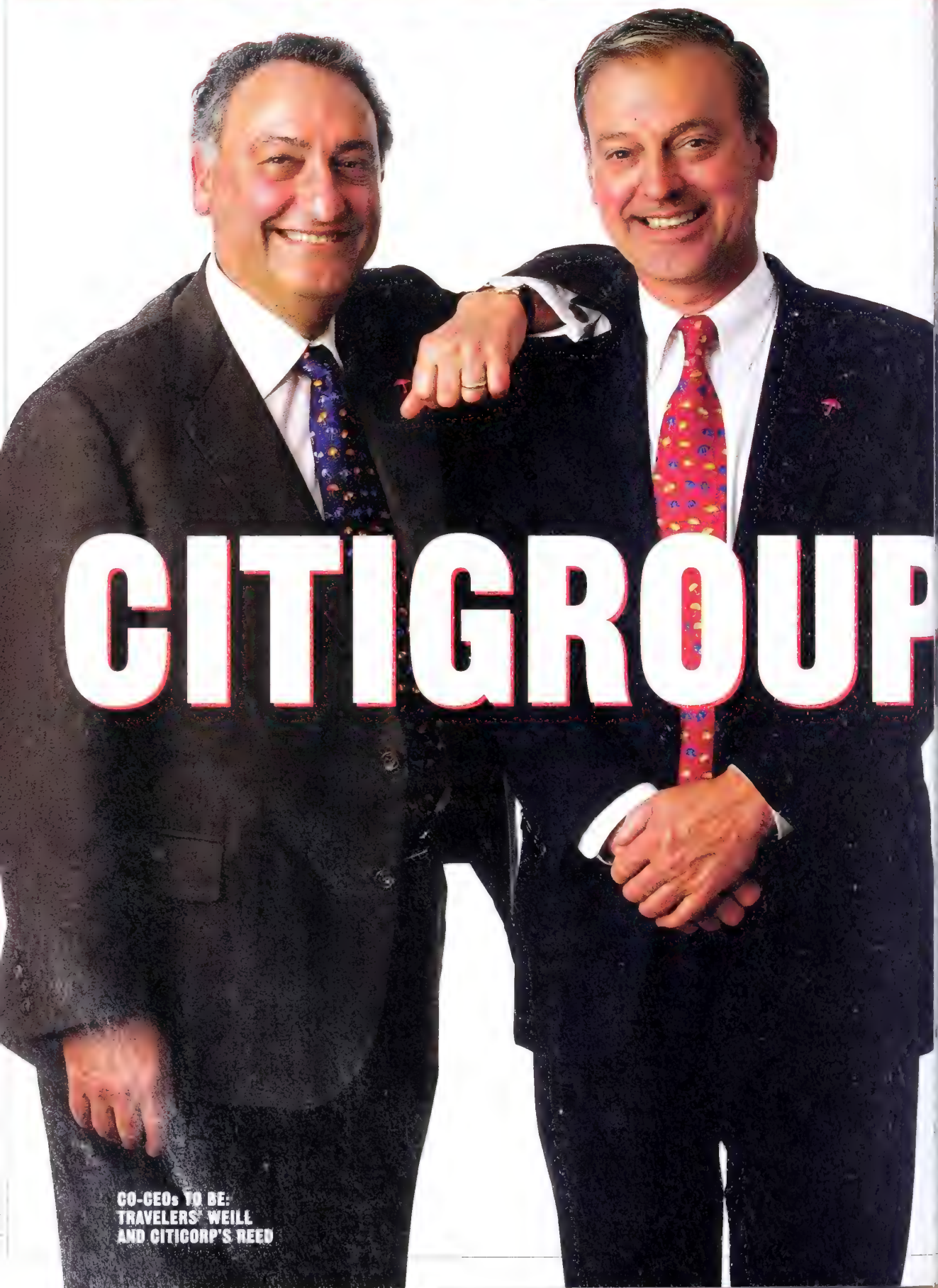
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H O N O R S



CO-CEOs TO BE:
TRAVELERS' WEILL
AND CITICORP'S REED

The Citicorp-Travelers deal may point the way to the future of financial services

Saudi Arabia's Prince Alwaleed bin Talal bin Abdulaziz Al Saud, who owns a staggering 40 million shares of Citicorp stock, admits to "feeling pretty good" about the world's largest-ever merger, the \$70 billion deal that will marry Citi to Travelers Group Inc. and create a megabank with global reach and \$700 billion in assets. He should be happy: The Apr. 6 group deal added some \$1.5 billion to the Prince's net worth. Says the Prince: "This is a very positive thing." The deal was also inevitable. In the U.S. and around the world, securities houses, and insurers are in the midst of a whirlwind of mergers and takeovers—all aimed at getting a grip on more and more of consumers' finances. Even before the deal, Citi execs were talking of reaching a billion customers worldwide by 2010. In creating Citigroup (page 37), the new to-be John S. Reed and Sanford I. Weill are only accelerating the transformation of the financial-services industry already under way (page 39). Says financial historian

Demographics are a key reason why this deal could work. The baby boomers of the U.S. and Western Europe are entering their 50s—their peak savings years. That is opening up vast opportunities for all sorts of financial firms to sell investment-management services and products. For example, paced by inflows into retirement-savings plans, U.S. mutual-fund assets already total \$4.8 trillion, and new money is coming in at a 30% annual rate. Indeed, a growing distrust of the world's retirement systems, many of them broke or nearly so, is boosting demand for mutual funds worldwide. So across Europe, Latin America, and even China, governments are beginning to set up privately funded retirement plans similar to the 401(k)s and IRAs of the U.S.

The growth of private retirement plans is increasing demand for new debt and equity offerings to fill those coffers. "The safety net is not adequate," says Ken Charles Feinberg, co-portfolio manager of the \$309 million Davis Financial Fund. "People will have to manage money for their retire-

Trust the start?

Chernow: "Mergers that looked like earthquakes last year now look like tremors by comparison."

Without waiting for Congress to change the regulatory environment, Weill and Reed are splicing together a global bank and an insurance, brokerage, and investment-banking giant. That could lead to a new age of global finance in which many distinctions between types of financial-service companies will evaporate.

But, of course, sounds like a new version of the financial marketplace (page 40)—a concept that has never really worked. Remember BankAmerica's unsuccessful purchase of First Union? Dean Witter Reynolds trying to sell stocks at Roebuck stores? Or Weill's abortive effort to meld his personal Loeb Rhodes brokerage with American Express? In the past, the idea of providing consumers and businesses the one-stop with a one-stop shop for financial services has not worked for some time—witness Deutsche Bank and the Swiss Bank of Switzerland—with unspectacular results.

But new forces could change the outcome this time. A worldwide convergence of societal changes, regulatory shifts, technological developments could make it easier for national financial-services firms such as Citigroup to acquire assets and distribute a variety of products tailored to local tastes. "This puts together products and channels under one roof with a global brand," says Mercer Management Consulting Inc. Vice-Chairman James A. Quella.

ments, and that's a great opportunity for whoever can tap it."

Citi is already the largest foreign financial institution in Latin America's private pension-fund business—and analysts think it will be able to expand its franchise there with Travelers' added heft. It has worked before: One reason why Merrill Lynch & Co. bought Britain's Mercury Asset Management Group PLC in 1997 was to gain global market share on the eve of the expected private-pension revolution. Just think how demand for new investments could expand further if the U.S. privatized a portion of Social Security or if Japanese savers start to move some of their \$10 trillion in bank savings into mutual funds.

Meanwhile, the boomers' demand for more investment options is helping force the convergence of financial products and industries around the world. Variable annuities, once the province of U.S. insurance agents, are now sold by stockbrokers. Insurance agents sell mutual funds, banks sell stocks, and brokers sell money-market funds that, in truth, differ little from checking accounts. German investors can now buy Fidelity mutual funds denominated in marks, and Japanese investors can charge purchases to Citibank Visa accounts that let them pay balances in dollars or yen.

Technology is also paving the way for one-stop financial shopping. Sophisticated databases now give financial firms detailed pictures of their customers' portfolios and spending and savings habits. That makes it possible to develop minute-

ly targeted sales pitches to be delivered by direct mail, phone, Internet, or even in person—for old-fashioned types.

However, technology could backfire on Citigroup. It will push mostly house-brand products while companies such as Charles Schwab & Co. follow the Wal-Mart Stores Inc. formula—efficiently distributing products from a range of manufacturers via an electronic mall.

And, increasingly, savvy investors are using the Net to find the best prices and deals. Already, 30% of all U.S. retail stock transactions are done via the Net, estimates Piper Jaffray Inc. analyst Bill Burnham. Little wonder that Toronto-Dominion Bank, for one, is building a network of discount and online brokers in Canada, the U.S., Australia, Britain, and Hong Kong. Its Waterhouse Investor Services Inc. unit is already America's third-largest online broker, and TD plans to use it to sell commercial-banking products as well.

FINANCE SITES. In time, nonfinancial players may also create virtual supermarkets, posing a threat to Citigroup's integrated model. That will require large investments in database marketing. McKinsey & Co. figures that a major U.S. bank must already spend \$1 billion or more every year on technology. But someday, consumers may find themselves buying mutual funds online at a finance store run by Yahoo! Inc. or Microsoft Corp. rather than from Citigroup or Deutsche Bank.

Still, there are millions of consumers around the world who aren't ready for online investing. Sweeping changes in regulation in many nations could produce a market of neophytes that would flock to a brand name like Citi. Japan, for example, has just launched its "Big Bang" financial-deregulation plan. Over time, it promises to scrap the numerous government rules that restrict consumers' choices, keep returns low, and direct savings to bureaucrats' pet industries. It also is providing an opening for foreign financial-services firms to woo savers from Japan's battered commercial banks and insurers. General Electric Capital Corp., for one, is teaming up with Toho Mutual Life Insurance to sell life and health coverage, while Germany's Dresdner Bank and Meiji Mutual Life Insurance Co. are managing funds jointly.

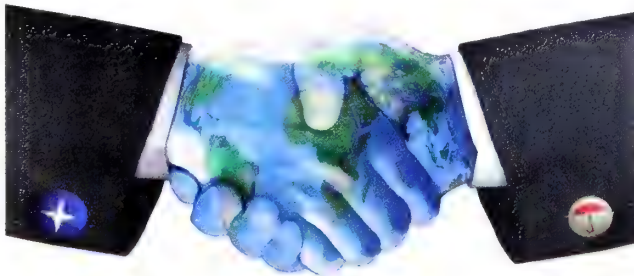
To enter markets in this fashion, it helps to be big. The proud papas of Citigroup are convinced that massive size and reach will be essential in the next decade. One reason is the burden of maintaining staggering arrays of global products. Take emerging-market privatizations. The initial public offerings they spawn are big favorites of individual and institutional investors around the world. And by all indications, they're likely to continue at a rapid pace. But to pull off and market costly privatization deals, argues Davis Financial's Feinberg, banks

and securities houses have to be able to demonstrate "unimpeachable financial strength." **MARGIN SQUEEZE.** Meanwhile, falling profit margins on common financial products—the result of competition and cheap distribution—make it harder to maintain that strength. For example, as mortgage lending has gone national over the past decade, the average spread between a long-term U.S. Treasury bond yield and a 30-year loan has fallen from 250 to 100 basis points. Margins will probably shrink in a similar fashion in Europe once the debut of the euro next Jan. 1 opens the way for more efficient market-

ing of products and more competition across national borders.

Declining margins on individual products are a major motivation to broaden product portfolios and attempt cross-selling. Any opportunity to capture someone else's product line and push it out through an existing sales force can result in immediate bottom-line gains. That's why some European banks see adding insurance and other products to their offerings as a new route to profits. For example, Credit Suisse already boasts a hefty retail-banking network in Switzerland and the global Credit Suisse First Boston investment bank. In December, it took over Swiss insurer Winterthur for \$10 billion. It now plans to market life, property, and casualty coverage from 80 Swiss-bank branches. Partly as a result of the deal, the market cap has soared 50%, to \$60 billion, in the past year.

In the U.S., meanwhile, bank mergers are creating a crop of likely players in the new financial-services arena. As barriers to interstate banking have fallen, superregional lenders such as NationsBank, First Union, Bank of America, and Wells Fargo have emerged. When these banks advance, the



One hitch for Citi: Online financial supermarkets may get to customers first

WHAT'S DRIVING THE FINANCE REVOLUTION

DEMOGRAPHICS

Baby boomers are reaching their peak saving years in North America and Europe. That's sparking a wave of competition for investments. A growing middle class in emerging nations will also need financial services.

DEREGULATION

Restrictions separating banks, brokers, and insurers are eroding in the U.S. Europe's single currency is opening opportunities for transnational financial services. Japan's "Big Bang" will promote competition.

GLOBALIZATION

The world is moving toward common standards of accounting, corporate governance, and market valuation, making it easier to sell products, such as mutual funds, that can be adapted to local tastes.

RETIREMENT

Faced with bankrupt or inadequate pension and health systems, consumers around the world are turning to private insurance and pension funds. That will further boost demand for stocks and bonds.

TECHNOLOGY

Computers, the Internet, and toll-free phone lines are all slashing the cost of delivering financial services, such as bill payment. Already, some 30% of all U.S. retail stock trades now take place on the Net.

bring new products with them. Alongside checking accounts, First Union pushes life insurance underwritten by American International Group, First Colony Life, and others. Citigroup's Reed and Weill want to extend the concept of universal banking even further. After all, why shouldn't U.S. customers be able to log on to a Citigroup Web site and buy non-IPOs, Travelers' life insurance, and Smith Barney investments, along with Citi CDs? By announcing their merger before Congress has passed legislation wiping out most of the restrictions on banks selling securities and insurance, Reed and Weill are "laying the gauntlet down as to what kind of reform there's going to be," says Credit Suisse Group Chief Financial Officer Richard E. Thornburgh. Will the Citigroup deal push Washington to finally update the law—after years of false starts? A U.S. Treasury official

notes that the merger would be allowed under financial-modernization legislation being pushed by the Administration. Federal Reserve Chairman Alan Greenspan also would be likely to support the deal in principle, though he has said he thinks reforms should be phased in more gradually.

The birth of Citigroup is bound to prompt more deals. Bankers, brokers, insurers, and other financial executives will see size as an index of future success. Right now, it would take Holland's ING Group, AmEx, Morgan Stanley Dean Witter, and Merrill Lynch to equal Citigroup's market cap. That doesn't mean they'll merge. But any combination seems possible as the realization sinks in that there are too many players to make the financial market of the future work.

By William Glasgall in New York, with John Rossant in Rome, Thane Peterson in Frankfurt, and bureau reports

THE 'COCA-COLA OF PERSONAL FINANCE'

The possible synergies of Citigroup are many, but so are the obstacles—laws, for instance

Perhaps the best word to describe the Citicorp-Travelers Group Inc. merger is audacious. John S. Reed, America's top banker, and Sanford I. Weill, America's top financial services dealmaker, on Apr. 6 proposed a \$1 billion merger that defies existing law. Banks such as Citicorp can't own property & casualty insurance, such as Travelers, and are limited in their ability to acquire brokerages. No matter what Reed and Weill believe that by acting aggressively, they can persuade legislators to knock down Glass-Steagall barriers and create a new kind of global financial paradigm.

It's a very gutsy move that only two men could make because they're taking a regulatory risk," says Jack H. Nusbaum, a partner at Willkie Farr & Gallagher. Former Federal Reserve Vice-Chairman Manuel H. Johnson Jr. says he was "amazed" by the audacity of the proposed merger.

LONG HISTORY. In addition to chutzpah, Reed, 59, and Weill, 65, are propelled by a shared desire to go out in a blaze of glory. Both are nearing the end of their careers and seem intent on making history by creating the first successful, fully integrated financial services behemoth. Says a close aide of Weill: "The last major thing we are going to do is to make this happen." Adds Reed: "We don't have to do this. We wanted to create this enterprise together."

Does it work? The agreement to create Citigroup came together in just five weeks, and many major decisions remain to be made. James Dimon, the co-chief executive of Travelers' Salomon Smith Barney, says he doesn't know what his job will be in the new entity. And Reed is still

learning the names of Travelers' businesses. For example, Reed mispronounced Primerica at the Apr. 6 press conference as "Prime America." Weill later good-naturedly chided him: "Remember, John, it's not two words."

But Weill, who aggressively wooed Reed, was able to sell the Citi CEO on the strong fit between the two companies. The logic of the deal is threefold. First, with \$698 billion in assets and \$48 billion in revenues, the new Citigroup will be the largest financial institution in the world. That will give it ample wherewithal to make further acquisitions and costly investments, such as building more elaborate computer systems. Being bigger also reduces its cost



of capital. "Size matters," says Gerard L. Smith, a managing director at Donaldson, Lufkin & Jenrette Securities Corp.

So does diversification. Combining the two institutions will make them less dependent on volatile earnings streams. Assuming the deal goes through, earnings of Salomon's trading operation, for instance, will fall from an estimated 17%-to-27% range of Travelers' operating earnings to about 8%-to-13%, estimates Sanford C. Bernstein & Co. analyst

Sallie L. Krawcheck. And Citicorp's Asian emerging markets income, which was 22% of earnings in 1997, will be only about 12% of Citigroup's earnings.

Finally, there is the central justification of the deal: cross-selling each other's products, mainly to retail customers. Over the next two years, Citigroup ought to be able to generate \$600 million more in earnings because of cross-selling, says Bernstein's Krawcheck. Citigroup hopes to double its \$7.5 billion in revenue in five years. "We want to be the Coca-Cola of personal finance for the ordinary American and to take that global," says

Deryck C. Maughan, co-chief executive of Salomon Smith Barney.

COMPLEMENTARY. The arrangement could solve Citicorp's and Travelers' biggest problems. Reed gets a stronger U.S. direct-sales force to market Citi checking accounts, mutual funds, and credit cards. In addition, while Citi has private bankers catering to the very wealthy, Travelers has 10,300 Salomon Smith Barney brokers, 80,000 part-time Primerica Financial Services insurance agents, and 100,000 agents that sell Travelers insurance.

At Travelers, Weill is drooling over Citicorp's 750 branch offices outside the U.S.; some 464 in Europe, 166 in Latin America, and 93 in Asia. Citi's global reach instantly transforms Travelers into an international player. Take Japan. Citi has enormously popular 24-hour automated teller machines and multicurrency savings accounts, and the bank is expected to win approval to link its 65 ATMs to the 20,000 terminals at post offices throughout Japan. Citi is already generating annual growth of 40% in Japan, Reed claims.

Travelers can also benefit from Citi's U.S. outlets. For example, "We have \$800 million of new mortgage origination each year," says Alvaro A.C. de Souza, an executive vice-president in North American consumer banking at Citi. "Twenty percent of that requires property and home insurance. Today we ask the customer, 'What is your insurance company?' In the future we will say to the customer, 'Here's an insurance package for you.'"

Citicorp's private bankers also offer clients such services as trust and estate planning, which Salomon Smith Barney doesn't have. For example, Dimon says a Salomon Smith Barney broker recently lost a \$20 million account because the company didn't have the expertise to value and set up an art trust for the client. It's a



business in which Citi's private banking group is expert.

On the institutional side, Travelers wants to build Citi's banking and trading relationships with 1,700 institutions all over the world. Citigroup, meanwhile, has a weak investment bank and does little equity underwriting. But Salomon Smith Barney is third-largest U.S. equity underwriter, and its investment bankers may be able to turn some of Citi's corporate clients into equity underwriting customers.

In the past, cross-selling has not paid off for most financial service companies—including the Citigroup partners. The

elers has had some success at Primerica Financial Services, but Citi has little to show for its efforts. "Has Citi effectively sold Citi banking products to their own credit card holders? The answer is no," says David S. Berry, a bank analyst at Keefe Bruyette & Woods Inc.

And there is great potential to upset the two institutions' web of partners and clients. For instance, Salomon Smith Barney's investment banking affiliate in Buenos Aires, Merchant Bankers Asociados, might pull out of the partnership because its asset management, private banking and bond trading activities overlap with Citibank's. Says Chairman Alejandro Reynal: "If the new organization is too large or inefficient, we will have to decide" whether to stay or leave.

Many other major issues haven't been addressed. For starters, Reed and Weill will almost certainly find it a challenge to run Citigroup together. Who will run both meetings? And who will get to put his candidates into top jobs? Will Weill have to sacrifice his intensely loyal general counsel, Charles O. Prince III, so Citicorp's crazy

erjack John J. Roche can navigate Citigroup through the formidable bank regulators? "If it works, it will be awesome," says one competitor. "But for three to five years, there will be lots of unhappy people."

The betting on Wall Street is that the co-CEO arrangement can't last, and that Weill and his close-knit team will eventually run the entire show. But a minority believes that Weill and Reed will sublimate their considerable egos and make it work. If they do, they may each be able to take credit for creating quite a revolutionary institution.

By Leah Nathans Spivey, with Debra Sparks, in New York; Andrea Mandel-Camacho, in Buenos Aires; Brian Brannan, in Tokyo; and Owen D. Mann in Washington

HOW THE PIECES FIT

	1997 REVENUES IN BILLIONS	
	CITIBANK	TRAVELERS
CONSUMER FINANCE	***	\$1.7
CORPORATE LENDING	\$1.2	***
CREDIT CARDS	\$6.9	NA
CASH MANAGEMENT	\$2.3	***
INVESTMENT SERVICES		\$21.5
INVESTMENT BANKING	\$1.6	
TRADING	\$2.5	
LIFE INSURANCE	***	\$4.4
PRIVATE BANKING	\$1.1	***
PROPERTY & CASUALTY	***	\$9.9
RETAIL BANKING	\$6	***

HIS MERGER WILL MAKE BIG WAVES

The creation of Citigroup makes other financial houses wonder if a takeover lies in their future

Ready or not, the race is on. The creation of Citigroup from the merger of Citicorp and Travelers Insurance Group is forcing every major financial institution in the world to check how its competitive position has changed. The banks, securities firms, and brokers all face a wave of mergers as they each scramble to keep up with the group's enormous array of products and its unparalleled worldwide presence. "Just sit back and watch," says Credit Suisse Group Chief Financial Officer Richard E. Thornburgh.



THIS DEAL UPS THE STAKES FOR RIVALS LIKE HONGKONG & SHANGHAI BANK (HSBC)

There are going to be more major transactions coming." U.S. regulations change and the deal goes through, the group model will influence financial-services markets worldwide. The \$698 billion behemoth, boasting a market capitalization of more than \$140 billion, is likely to be the first of several new financial giants formed in the U.S. from insurance companies, banks, and brokerage houses as they jockey to maintain competitive levels of capital. **MARKETS.** Even giants such as Merrill Lynch & Co. and Morgan Stanley Dean Witter & Co. have their worries. Do they now need a tie-up with a commercial bank to gain more local and access to corporate clients? If they forgo such a tie-up, will they see their deal flows dry up? Meanwhile, U.S. banks such as Chase Manhattan Corp. and Citicorp are probably wondering whether they need to create securities firms to create products to sell to their cus-

tomers. McKinsey & Co. estimates that U.S. lenders have excess capital to finance \$1 trillion worth of deals. In ballpark numbers, that means the top 100 American banks could gradually shrink to a mere seven.

Outside the U.S., the impact of the Citigroup merger is likely to be strongest in the world's emerging markets. It's in Asia and Latin America that Citicorp has already carved out substantial market share by targeting the savings of an expanding middle class. Citigroup says it will consider major insurance deals in emerging markets, where the business accounts for just 2% of gross domestic product, compared with 8% in the U.S.

Citicorp CEO John S. Reed and Travelers' head Sanford I. Weill are especially interested in Asia, where Citi is already the most sophisticated player and where financial turmoil has created fresh opportunities for expansion. That ups the stakes for competitors such as HSBC Holdings PLC and the Japanese banks. HSBC will have to keep pumping money into technology and new offerings. In Japan, fear of losing customers to Citi's one-stop shopping may force Japanese firms to consider new alliances with foreign partners, says Keiko Honda, a McKinsey consultant in Tokyo.

SPACE RACE. Not all institutions in Asia see the Citigroup combine as a threat. "Citigroup will be a very formidable financial supermarket," says Marc Sylvain, managing director of Fidelity Investments in London. "That is good news for top mutual funds, who can fight for space" on Citi's shelves. Fidelity, which already distributes through Citi in Southeast Asia, figures its funds may gain new prominence as the newly formed Citigroup spreads its distribution channels.

THE FALLOUT

BROKERS AND MONEY CENTER

BANKS Banks such as Chase and J.P. Morgan may need to merge with each other or with brokers such as Merrill Lynch.

INTERNATIONAL BANKS Their franchises look less impressive when compared with Citigroup's. Banks such as Deutsche Bank may look for partners in the U.S.

INSURERS Companies such as Germany's Allianz are waiting to see if the U.S. repeals barriers to combining banking and brokerage services. If so, they would shop for U.S. acquisitions.

DATA: BUSINESS WEEK

For the most part, however, Citigroup's role will be as a catalyst and a model for change. For example, neither Travelers nor Citi is a big player in Europe. But together, Reed and Weill think they can gain ground as the consolidating European financial services industry prepares for the introduction of a single currency in 1999. Citi's relatively customer-friendly approach is already a big hit in Germany, where giants such as Deutsche Bank risk losing ground if they continue to take clients for granted. "If a customer goes in to [a Deutsche branch] saying he wants a loan for a child's wedding, the banker may give him a lecture on why he hasn't planned for it sooner," jokes Reed.

Reed and Weill may be smiling. But it's likely to be some time before their competitors will be in a laughing mood.

By Stanley Reed in London and Kerry Capell in New York, with Thane Peterson in Frankfurt

COMMENTARY

By Peter Coy

GREAT BIG COMPANY. GREAT BIG MISTAKE?

There they are, John Reed and Sandy Weill, wind in their hair, standing on the prow of a giant, unsinkable ship and gazing into a limitless future. On Wall Street, no superlative is too ripe to describe the genius of the proposed merger between their companies, Citicorp and Travelers Group Inc. Why, did you know that Citigroup will have more assets than any other financial-services company in the world? Did you know it will have 100 million customers? The greatest strength of this deal is its sheer size.

Its size, however, also may prove to be its greatest weakness. In finance, as in seafaring, bigger is not always better. Assets can be a heavy weight to bear when they underperform. Citicorp itself was at death's door as recently as 1991 when bad loans torpedoed earnings, its stock sank to single digits, and Reed was sounding out potential rescuers.

Why are these two big companies becoming one really, really big company? Weill and Reed are betting that they can gain what is quaintly known as "share of wallet" by creating a worldwide brand and a full gamut of homemade products and services. Their big idea is to use Citicorp's branch network to sell products from Travelers such as insurance and Smith Barney Inc.'s brokerage service, while using Travelers sales agents to push Citicorp products, such as credit cards. For that strategy, scale and breadth are essential.

But there is another way to offer a supermarket of financial services that could make Citigroup look archaic before it gets its first letterhead printed. Instead of trying to be all things to all people, companies such as Charles Schwab & Co. position them-

selves as trusted intermediaries, providing a menu of the best financial products available from all sources. The companies whose products the distributor sells focus on doing one thing well, whether it's mortgages or credit cards.

Then there's the Internet, which also undercuts the advantage of big-



HAPPY DAYS AHEAD? The idea of a financial supermarket may be undercut by Internet technology

ness. Consumers are finding gobs of up-to-date market information and access to all manner of financial services on the World Wide Web. Mouse in hand, they're ferreting out good deals, regardless of how big or small the supplier is. Look at the success of Web sites that allow comparison shopping for insurance and mortgages, or online stock-trading firms like Web Street Securities, Datek Online, and E*Trade Securities Inc.

Customers of Palo Alto (Calif.)-based E*Trade don't mind that it lacks a skyscraper in Manhattan with a giant red umbrella on the side.

What they like is that E*Trade charges \$14.95 to trade 800 shares of a \$20 stock, vs. a \$359 commission at Smith Barney. "In this new virtual community, size matters not," says E*Trade president Christos M. Cot-sakos. Neither, he says, do many names and symbols that evoked fuzzy feelings in past generations: "Some of

the older brands just don't resonate with the Gen-Xers and baby boomers. A megamerger's not going to change that."

AMEX, ANYONE? Also, for all the grand visions, financial supermarkets have an inglorious history. Citicorp's original attempt failed expensively on Reed's watch, and Weill was associated with a similar mess at American Express Co. in the 1980s that he wishes people would forget.

Of course, it's possible that this time will be different. For customers who don't like to shop around—and don't mind having all their eggs in one basket—Citigroup may be able to charge a tidy premium for a branded, customized bundle of products.

But it will take years for Travelers and Citicorp to work together as a single marketing machine. Gigantic computer sys-

tems must be merged. And managers who are accustomed to maximizing the profit of particular lines of business will need to be reeducated to support cross-product promotions. "You need compensation incentives internally to do it the right way," says James A. Quella, a fan of the deal who is a vice-chairman of Mercer Management Consulting Inc.

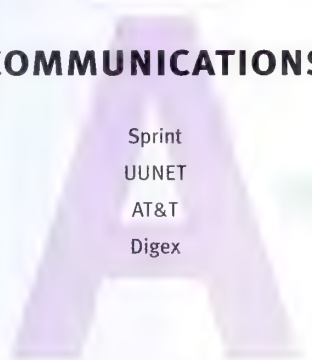
Citigroup will be big and powerful, all right. But it also will be extraordinarily difficult to steer. And icebergs lie ahead.

Coy is associate economics editor.

HOW TO IMPLEMENT A VIRTUAL PRIVATE NETWORK WITHOUT A VIRTUAL VENDOR NETWORK.

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THE ECONOMY

CONSUMERS HAVE MONEY TO BURN

It has been decades since there were such good reasons to splurge

It's lucky that the story of the economy isn't headed for the silver screen, because the best title, *As Good As It Gets*, is already taken.

Ask any consumer—say, Kimberlee A. Morehouse. In early April, she and her husband, Brian, bought a brand new four-bedroom home for \$198,000 in the historic mining town of Georgetown, Colo., 45 miles west of Denver. They then plunked down \$1,500 in cash on a new four-piece bedroom set. "We bought exactly what we wanted," says Kim, hinting that more big-ticket purchases are planned. The couple—he a heavy-equipment mechanic, she a clerk in the state court—isn't worried about their job prospects or paying off their mortgage. The economy "is very strong right now," she says. "I feel very secure."

So do most Americans. The latest survey by the Conference Board shows that consumer confidence is the highest in three decades. The result: Shoppers are spending at the fastest rate of this decade. Economists figure real consumer spending rose at a torrid 5.5% annual rate in the first quarter. Shoppers see an Eden of full employment, income and stock gains, low interest rates, and low prices on everything from cars to camcorders.

The buying binge is stoking America's expansion as it enters its eighth year. Thanks to brisk home sales (page 30) and other consumer purchases, real gross domestic product likely grew at a 3.5% annual rate in the first quarter—a

very peppy pace this late in an expansion. "Rising jobs and incomes produce a willingness to spend while cheap imported goods and low interest rates boost the ability to spend," says Bill Cheney, corporate economist at John Hancock Cos. "The willingness and ability feed on each other." The cycle has put Wall Street in a cheery mood, too—sending the Dow Jones average over the 9000 mark on Apr. 6.

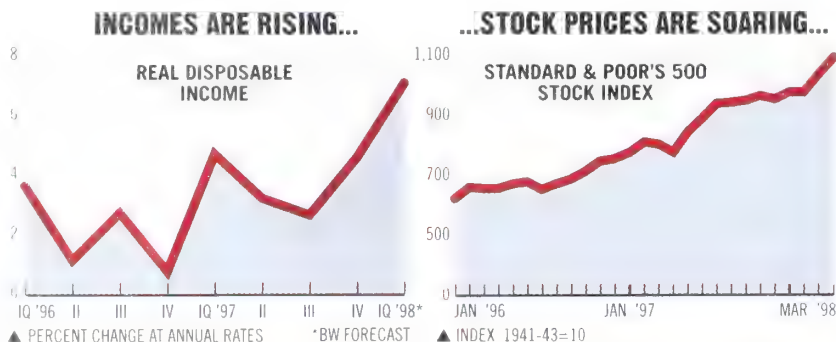
The economy's dependence on consumers does have its risks, however. Right now, households have every reason to feel secure. But a sudden shock, such as a big drop in stock prices, could cause consumers to feel less wealthy and snap shut their pocketbooks, leaving businesses with too much inventory and too many workers.

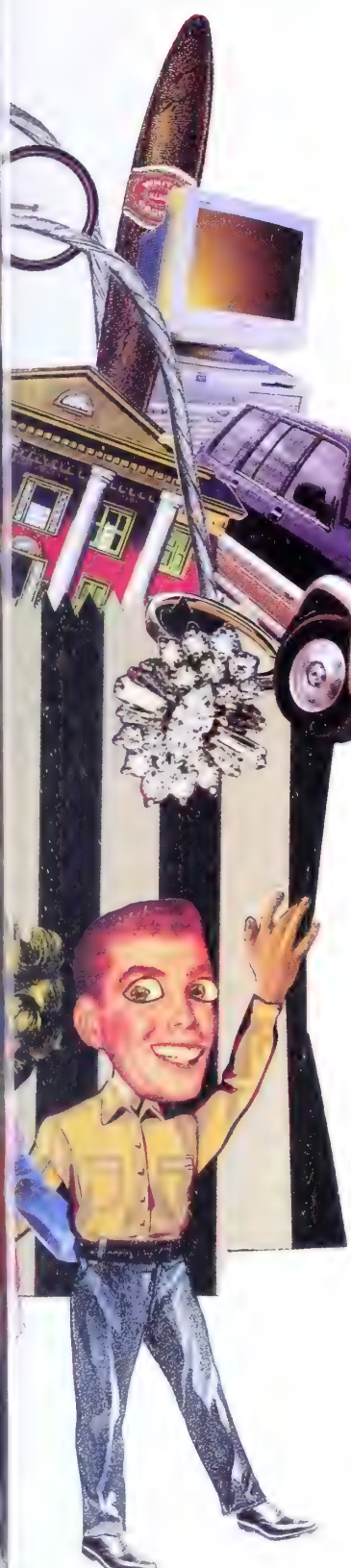
RATE HIKE? Another risk is that all this buying becomes too much of a good thing. For now, consumers are avoiding the dangers of the 1980s when excess demand generated a debt overhang and rising inflation and interest rates. But the economy could still overheat: Hot domestic demand could roll right over the drag from Asia. And more competition for workers could push labor costs above the gains in productivity. In the fourth quarter, for example, productivity grew at a 1.5% annual rate, and unit labor costs climbed a steeper 3.3%. If that trend continues and businesses start raising prices, the Federal Reserve could slam on the monetary brakes.

The good news is that the second



WHY AMERICANS ARE ON A SPREE





quarter may show a more moderate—and sustainable—trend with real GDP rising 2.5%. The mild winter caused by El Niño got people out shopping and allowed builders to start new housing ahead of schedule. Already, the return of normal weather crimped March employment and retail data (page 31). But even with a drop of 36,000 jobs in March, payrolls grew by 205,000 a month in the first quarter, keeping the unemployment rate at a low 4.7%.

Meanwhile, consumers have more cash to spend. Real aftertax income probably rose at a 7% annual rate in the first quarter, the biggest gain in five years. Steady pay raises prompted Peaches Herder of Philadelphia to buy a new Chrysler Cirrus to replace her Mercury Sable. There was nothing

wrong with the six-year-old car, but Herder says having the extra money gave her the itch for new wheels.

The Cirrus “caught my eye, so I bought it,” says the 57-year-old drug counselor.

In addition, paychecks can go a lot further in 1998, thanks to an inflation rate of just 1.4%.

Also, even though the median price of a new home rose 7.3% in February, low mortgage rates let more families afford a home. Combined new and existing home sales hit a record high seasonally adjusted annual rate of 5.6 million in February. The gain in home prices is allowing owners to take out home-equity loans to use for vacations, college tuition, or computers. Such loans are up 15.4% from a year ago.

Finally, the stock market’s bull run continues to build household wealth. Economists at Regional Financial Associates Inc. figure that the stock runup so far this year has added an average of \$3,700 to household net worth. That’s on top of the \$14,900 gain created in 1997.

More income and wealth are keeping debt loads manageable. Even though installment credit jumped \$7 billion in February, debt outstanding stayed at 20.4% of disposable income, down from the record 20.8% hit in late 1996.

In short, consumer fundamentals are the best in a generation (charts). After years of job jitters and watching pennies, consumers are spoiling themselves. Allen Baker and his wife, Suzanne Frey, are sparing little expense to build their dream house in Wasilla, Alaska. A 6.5% mortgage rate enabled them to borrow more than they had expected. So they have already spent \$4,000 on new kitchen and laundry appliances. And they’re prepared to spend an additional \$20,000 for other white goods and fixtures, right down to door latches. A new house, Baker says, “turns you into the ultimate consumer, thinking about things you never dreamed you’d think about. I mean, door latches?”

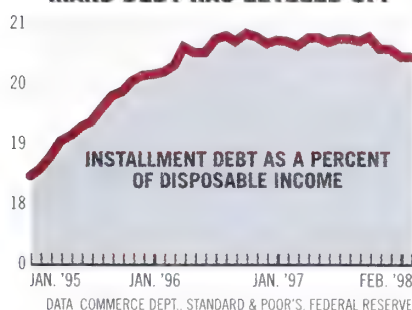
“GOOD DEALS.” Could consumers revert to their overindulgent 1980s habits? Back then, strong demand helped to push the core inflation rate from 3.7% in 1987 to 4.7% in 1989. The Fed responded by hiking its federal funds rate from 5.8% to close to 10%. Luckily, the 1990s seem a different era. “Consumer surveys show people are very sensitive to price,” observes David H. Resler, chief economist at Nomura Securities Co. Resler says consumers are shopping with gusto now because they view their purchases as “good deals.” And they are smarter about using debt, paying off more quickly and shopping around for low interest rates.

The unknown, he says, is what happens when businesses lift prices to make up for higher labor costs. After all, rising wages mean that businesses are paying more for labor, which is cutting into profits. Across the economy, profit margins fell in the fourth quarter for the first time in almost three years. Productivity gains help, but at some point, profit-hungry companies will try to raise prices and make the hikes stick.

How consumers react is the key to growth, inflation, and Fed policy. For now, cheap imports from Asia will hold down goods inflation, so the Fed is unlikely to react with the vehemence it did a decade ago. That makes it very likely that the expansion will continue to produce solid growth, low inflation, and further income gains. For consumers, that really is as good as it gets.

By Kathleen Madigan in New York, with David Lindorff in Philadelphia and bureau reports

...AND DEBT HAS LEVELLED OFF



REAL ESTATE

IF YOU BUILD IT, THEY WILL POUNCE

Buyers' demand for pricey houses seems insatiable

If you don't think the market is hot in Austin, Tex., ask Gerald Lamar. Demand for \$500,000 houses in the city's booming high-tech economy is so strong that of the dozen such homes he has put up in the past 12 months, nine were completed "on spec"—before finding a buyer. Says Lamar, co-owner of Lamar Homes Inc.: "We're selling whatever we can put in the ground."

Lamar is not alone. With the economy soaring and new houses selling at a record pace nationwide, Lamar and other developers are scrambling to meet seemingly insatiable demand. The buying frenzy has pushed the inventory of new homes to its lowest level on record: At the current rate of new-home sales, it would take just 3.8 months to sell all the available houses on the market nationwide (chart). That tight housing market has more builders—particularly those working in high-end segments (\$500,000 and over) in places such as Atlanta, Chicago, Los Angeles, and Miami—doing what Lamar does: Build first, sell later.

"SCARED TO DEATH." Isn't building on spec risky? Didn't it contribute to bankruptcies and depressed real estate markets in many of the same cities when the 1980s economic expansion faded? You bet. And that's why some real-estate observers are growing concerned. "It's hard not to get excited. The economy is strong, and everything looks great, but I hope people don't get carried away [with spec building]," says David F. Seiders, chief economist at Washington's National Association of Home Builders. "If the Asian economy doesn't slow down the [U.S.] economy, the Feds probably will." Says Harry Savio, senior vice-president at the Texas Area Capitol Builders Association: "We see guys putting up \$1 million spec homes like they did back in the '80s. If I were them, I'd be scared to death."

Indeed, Seiders estimates that sales will fall to an annually adjusted rate of 750,000 by the fourth quarter,

down some 12% from the first quarter. "The first quarter is going to be the high point of the year," he predicts.

Such talk doesn't unnerve builders like D.R. Horton Inc., an Arlington (Tex.) developer that recently upped its speculative-home building program by 22%, to 55% of its business. Horton sees little risk when demand is so strong in Houston, Phoenix, and localities in Southern California. Ditto for Barry Carroll, chairman of Carroll International Corp., a Des Plaines (Ill.) developer that is putting up several \$600,000 to \$800,000 spec houses in Lake Forest, a fashionable Chicago suburb. He says the houses are "sold before they're finished—within six months of breaking ground."

Developers aren't the only ones betting on building in a strong economy. In New York City, the owners of a co-op apartment at 119 W. 71st St. are building a luxury, three-bedroom penthouse on the roof of the nine-story building. While the group does not have a buyer yet, it's betting it will by the time the project is completed later this year—and will make a profit. "In this environment, we can be more speculative. We're very confident about finding a buyer," says Robert J. Warshaw, a partner at investment-banking firm Lazard Frères & Co. and president of the co-op board. "In a different environment, we might not take the risk."

Indeed, this time around, speculative building might not get out of hand. For one thing, real-estate agents and economists



ON SPEC As the economy soars, one Texas builder says: "We're selling whatever we can put in the ground"

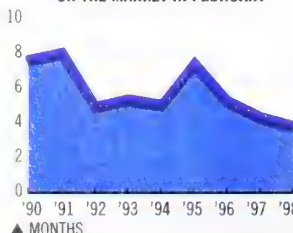
say so far they don't see the excess speculative activity that was rampant in the '80s. And equity isn't flowing as freely as it was back then, when spec housing was popping up everywhere, and banks and savings and loans offered 100% financing, seemingly to anyone with a blueprint. Now, financial backers are demanding builders have equity in the projects, hoping to encourage restraint.

More than anything, though, builders say they have learned from the past. "We went through the '80s downturn, and it was very, very hard—like a death in the family," says Lamar, the Austin developer. "We lost everything. I'm very cautious—everyone's very cautious these days." Meanwhile he's lining up financing for as many as 10 new spec homes this year.

By Stephanie Anderson Forest, Dallas, with Ann Terese Palmer, Lake Forest, Ill.

A SELLER'S MARKET

SUPPLY OF NEW HOMES
ON THE MARKET IN FEBRUARY



▲ MONTHS

DATA: NATIONAL ASSOCIATION OF HOME BUILDERS,
U.S. BUREAU OF THE CENSUS

\$250,000 (per child) — with

this child will likely cost its parents — college included — over the next 21 years. But the future

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COMMENTARY

By Richard S. Dunham and Howard Gleckman

BIG TOBACCO'S HARD LINE WON'T SOFTEN CONGRESS

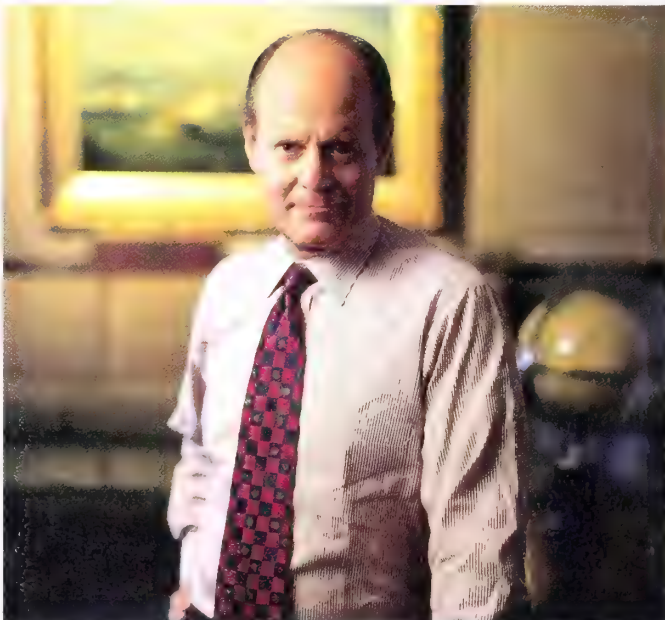
On Apr. 8, RJR Nabisco Inc. CEO Steven F. Goldstone tried to drive a stake into the heart of a tobacco deal now wending its way through Congress. "This legislative process is broken beyond repair," an angry Goldstone told a lunchtime audience at the National Press Club. But if he thought that pulling out of tobacco talks would kill anti-smoking legislation, he badly miscalculated.

Although other tobacco companies quickly followed Goldstone's lead, the industry's hard line may backfire. Instead of snuffing out a tobacco bill, the industry walkout will only change the form of the final measure—and not to its liking. "There is overwhelming bipartisan sentiment to pass legislation to stop the industry from going after kids," says Representative Henry A. Waxman (D-Calif.). "The tobacco companies are not as powerful as they once were."

That's for sure. Rather than intimidating lawmakers, the cigarette makers' counteroffensive has only hardened their resolve. Within hours of Goldstone's bombshell, all the key Washington players rushed to declare anti-tobacco legislation very much alive. "We cannot be blackmailed or cajoled by the tobacco industry," fumed Senate Commerce Committee Chairman John McCain (R-Ariz.), whose \$506 billion measure was approved by his panel on Apr. 1. A grim President Clinton challenged the industry to reverse course. "We're going to get this done," he said. "Now, they can be part of it, or they can fight it. But I think they ought to be part of it."

Even tobacco's longtime defender, House Commerce Committee Chairman Tom Bliley (R-Va.), was quick to reject the industry's effort to pull the plug on a deal: "Efforts in Congress to reduce teenage smoking are not dead. I hope Congress will ultimately agree on a tough, bipartisan plan."

Now, lawmakers predict that Congress will go ahead with a narrower bill. It likely will grant the Food & Drug Administration sweeping new powers to regulate tobacco, fund new programs to combat youth smoking, raise excise taxes on cigarettes by at least \$1.10 per pack over five years, and use some of the proceeds for a middle-class tax cut.



Without industry cooperation, however, some provisions can't become law. These would include penalties if youth-smoking-reduction targets are not met, and restrictions on tobacco marketing and advertising. Because of First Amendment concerns, those curbs would likely be struck down by the courts unless the industry consents to them. "It seems to be silly season in Washington if they think they can pull this off effectively without tobacco," says Mississippi lawyer Richard F. Scruggs, a key negotiator of the deal between the industry and the states.

But a walkout deprives Big Tobacco of the one thing it craves most: some protection against lawsuits. Indeed, if it's serious about abandoning the legislative process, the industry would break one of the cardinal rules of Washington: Never take yourself out of the ball game.

Goldstone's move also could be a PR

disaster, opening the industry to allegations that it cares more about its bottom line than children's health. Tobacco's worsening image would force even once-sympathetic congressional Republicans to take a hard anti-tobacco line lest Democrats paint them as industry lackeys next fall. "In a counterintuitive way, this (walkout) increases the chances of legislation,"

RJR CEO GOLDSTONE

Rather than killing the tobacco deal, his exit from Capitol Hill talks may strengthen lawmakers' resolve to pass a bipartisan bill

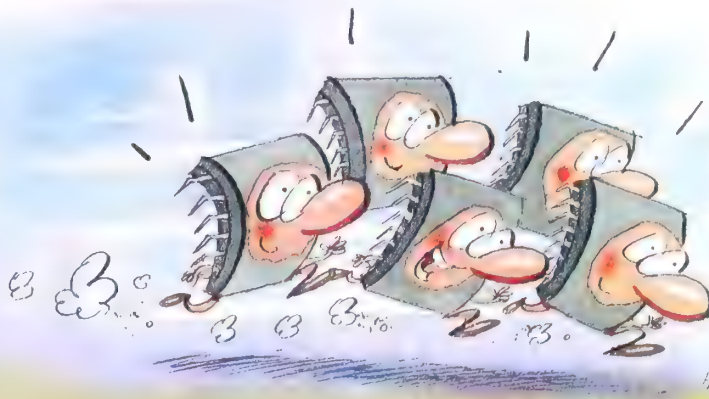
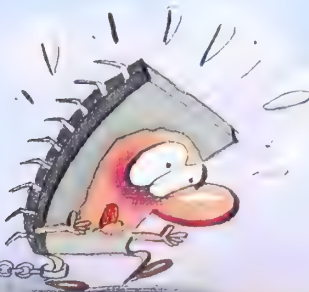
says former FDA Commissioner David A. Kessler, now dean of the Yale School of Medicine. "No one likes being bullied."

Many Washington hands think Goldstone's dramatic announcement was simply a negotiating ploy. "The industry is bluffing," snaps one key Senate staffer. Tobacco's strategy may be to pressure Congress to move

away from McCain's proposal—and back toward last year's proposed \$368.5 billion settlement.

That's what Goldstone is counting on. RJR is so highly leveraged that Wall Street analysts say McCain's bill could jeopardize its financial viability. But Goldstone finds little sympathy on Capitol Hill, where tremendous momentum exists for tobacco legislation—with or without industry participation. "We didn't put them in this financial situation," says a tobacco ally on the Hill. Goldstone readily admits, "I know precious little about the way this city works." What he does know is that with the cost of the tobacco bill rising, investors have been dumping his company's shares. In the end, his walkout may do little to change that, either.

Dunham and Gleckman follow the ups and downs of tobacco legislation.



IPS

IS IT POSSIBLE? BUM CHIP FROM INTEL?

Low-cost Celeron, due Apr. 15, is already the butt of jokes

Intel Corp. isn't used to flops. Sure, not all of its chips have been as popular as the Pentium, which has sold millions of units since its introduction in 1995. But for the past two decades, Intel has mostly rolled out new PC processors to market acclaim—and then reeled in juicy profits from buyers ravenous for more PC power.

Until now, that is. The company's new low-cost Celeron chip, set to be introduced on Apr. 15, is already the butt of jokes. Online message boards are clogged with mocking references to the "Celery." When an advance look at a Celeron by *PC World* magazine revealed sluggish performance, gleeful taunts flew and the Internet within hours—and by the news, Intel's stock has dropped. Even Brian L. Halla, chief executive of rival National Semiconductor Corp., nicknamed the chip "Deceleron."

CORNER. The object of this derision: A stripped-down version of Intel's Pentium II processor aimed at the burning sub-\$1,200 PC market. Intel meddled up the Celeron to take back market share from companies such as National Semiconductor and Advanced Micro Devices Inc. The competitors' Pentium-compatible chips have seized the low-end market—compared to just 4% in more expensive markets. But if early reviews are an indication of its fate, the 266-megahertz Celeron is unlikely to knock off the Pentium. "It's a dog," sniffs analyst Drew H. Cowen & Co. Responds Paul Cellini, head of Intel's processor unit: "The Celeron is optimized for basic needs."

What went wrong? Intel got painted into a corner last fall, when PC prices cratered just as the chipmaker was trying to move PC buyers to the pricey Pentium II. The Celeron is a compromise to target cheap PCs with a Pentium II-type processor. To cut costs, engineers pulled out memory chips included in the Pentium II, but the move hurt performance by 27%, according to *PC World*'s tests.

That's translating into lukewarm response from PC makers. Some, including Compaq Computer, Hewlett-Packard, Packard Bell NEC, and startup Monorail, are planning to deliver \$999 Celeron-based PCs. "Intel will put a substantial amount of marketing muscle behind Celeron," says Andrew Watson, marketing vice-president for Monorail Inc. But others are biding their time: IBM and Toshiba say they haven't committed, and Digital Equipment Corp. says it could pass entirely, in favor of the K6 chip from AMD. NEC, which isn't using the chip in its corporate line, sounds a common refrain: "We are very concerned about the price performance," says Executive Vice-President Luis F. Machuca.

That could leave Intel red-faced. Analysts expect it to sell just 5 million to 6 million Celeron chips this year, around 10% of its sec-

ond-half output and just one-third of the cheap-PC market. Meanwhile, rivals are gaining. National already sells the \$80 MediaGX processor used in \$799 Compaq models and on Apr. 6 disclosed plans to sell a cheap "PC-on-a-chip" that could be used by 1999 in PCs costing only \$400. The next day, AMD told analysts that it has licked the production problems that throttled production of its K6 chips. The company now says it will build 12 million K6s this year for customers such as IBM and Compaq.

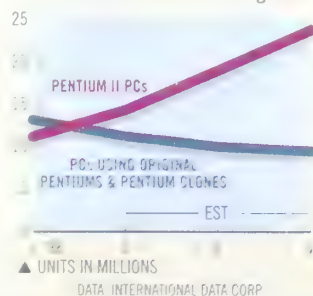
SPEEDING UP. Even if the Celeron bombs, Intel won't suffer too badly. Many PC makers will use it in some models, if only to placate the king of chips. And Celeron is just the first step in Intel's yearlong plan to force the PC market to Pentium II-type PCs. On the same day it launches Celeron, Intel is adding new 350- and 400-MHz Pentium IIs aimed at PCs priced over \$2,000. And by this fall, Intel will ship a faster Celeron, code-named Mendocino. Meanwhile, the shift continues to the Pentium II, which has a proprietary connection that clones don't have. By the fourth quarter, predicts International Data Corp., 72% of PCs will be based on the Pentium II architecture—all using Intel chips.

Intel's biggest challenge may be in convincing PC makers and customers that Celeron makes the grade. Intel says it's using the Celeron name because it did not want to "dilute" the Pentium brand, says Kelly Henry, an analyst with IDC. "That says to me they think of it as an inferior product," she adds. That's a message that the market seems to have grasped.

By Andy Reardon
in San Mateo

ACCELERATING

The Celeron may not be a sizzler, but other Pentium IIs are doing well



MEDICINE

THWARTING CANCER

Designer estrogens may be blockbusters—with risks

The war on cancer has moved to a new front: For the first time, a drug has been found to prevent cancer. On Apr. 6, the National Cancer Institute (NCI) announced that, after four years of a huge clinical trial, the breast cancer treatment tamoxifen reduced the incidence of the disease in high-risk women by 45%. V. Craig Jordan, director of the breast cancer research program at Northwestern University, says he will report similar findings on May 17 from a two-year trial of Eli Lilly & Co.'s raloxifene, an osteoporosis treatment.

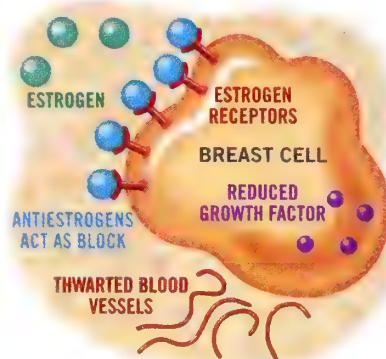
Both medicines belong to a group of drugs commonly called antiestrogens, or "designer" estrogens. These compounds take advantage of the fact that cells in different parts of the body have different receptors for the estrogen hormone. They block the receptors in breast cells, where estrogen can cause cancer, while increasing receptivity in bones, where the hormone builds mass.

Zeneca Group PLC's tamoxifen, introduced 20 years ago, is the first generation, but a second is coming, and drug analysts are predicting blockbuster sales. An estimated 29 million U.S. women are at high risk of developing breast cancer, and 18 million women suffer from osteoporosis. Merrill Lynch & Co. estimates that annual sales of raloxifene, approved last December, will reach \$2.7 billion in a few years. "The opportunities here are equivalent to those created by penicillin as the first natural antibiotic," says Jordan.

BLASTED. Doctors, however, caution that these drugs may not be for everyone. In fact, on Apr. 7, British researchers blasted the NCI for cutting its study short by two years, saying the extra time would have provided more definitive data on risks. Even with the early cut-off, the NCI study found that tamoxifen increases the risk of cancer in the endometrium lining the uterus. The new designer estrogens work

RUNNING INTERFERENCE

Antiestrogens block cancer-causing estrogen from binding to the cell.



The drugs also reduce growth factor, a blood vessel stimulant, so nourishment can't reach a developing tumor.

slightly different than tamoxifen, as so may be said. Schering-Plough's toremifene, approved for breast-cancer treatment in December, shows a low risk of endometrial cancer in rats, but has yet to prove a safer in people than tamoxifen. Researchers say raloxifene shows no evidence of causing endometrial cancer in women so far, but Aman U. Buzdar of Houston's M.D. Anderson Cancer Center cautions tamoxifen

was in use for 10 years before its link with endometrial cancer was discovered.

Other designer estrogens in clinical trials include Smithkline Beecham's idoxifene, Pfizer Inc.'s droloxifene, a compound from Lilly called serm-3, and Zeneca's faslodex. The Food & Drug Administration has yet to approve any for breast cancer prevention, including tamoxifen. But as news of the recent studies spread, plenty of women are certain to start asking about them.

By Catherine Arnst in New York

PHILANTHROPY

OSCAR, MEET GEORGE

A flashy award for corporate giving is about to debut

Corporate philanthropy often means writing a check or buying a table at a charity ball. But for Aaron Feuerstein, owner of Malden Mills Industries Inc. in Lawrence, Mass., it meant keeping workers on the payroll for months as he rebuilt his fire-razed plant.

Feuerstein is one of 10 corporate heroes who are in the running for the first annual Newman's Own/George Award. Actor Paul Newman, who founded the not-for-profit Newman's Own food company, and John F. Kennedy Jr., president of *George* magazine, will present the award on Apr. 13 for innovative and

significant corporate philanthropy. A \$250,000 check from Newman's foundation will go to the winner's favorite charity. Sony Electronics is giving \$250,000 over the next two years to the awards.

Among those winnowed from 400 applicants are Norwest Corp., the Minneapolis bank that is providing \$300 million in low-interest mortgages and giving Habitat for Humanity International \$16.5 million to build 50,000 homes. EBSco Industries Inc. in Birmingham, Ala., made the list by raising \$10 million to help revive the Alabama Symphony.

TEN FINALISTS

CITIBANK

EAST CAROLINA BANK

EBSco INDUSTRIES

HANCOCK COMMUNITIES
AND THE MARTZ AGENCY

KIMBERLY-CLARK

MACY'S WEST

MALDEN MILLS

NORWEST

PATAGONIA

WORKING ASSETS
LONG DISTANCE



This celebration comes just when some politicians and investors are demanding more disclosure about corporate charity—a move that some in the philanthropic community claim could curtail giving. "[Philanthropy] has succeeded as part of a company's PR or marketing strategy, or the money should be paid out in dividends," says shareholder activist and investor Nell Minow, a principal in Lens Group.

The critics cut little ice with JFK and his leading givers. "It would be great if business competed for this award and didn't run afoul of shareholders," Kenney said. Norwest Chairman Richard M. Kovacevich is vehemently opposed to disclosure. He says the 1.7% of pretax income that Norwest spends on such ventures as Habitat or low-interest mortgages is "an investment in our communities. Admittedly, it is hard to quantify [the payback], but so is marketing, advertising, even technology."

By Richard A. Melcher in Chicago

INTRODUCING THE "BIG TWO" IN CONSULTING.

It doesn't
matter
who merges,
splits or gets
taken over,
the choices
will still be
the same.

EDITED BY PAT WECHSLER

DUPONT ADJUSTS THE CHEMISTRY

WILLIAM HOLLIDAY IS SURE wasting no time putting his mark on chemical giant DuPont. The CEO since February, Holliday announced on Apr. 7 an organizational overhaul that will let the company focus on faster-growing businesses. This reorganization could signal bigger changes ahead, including possible spin-offs. Bear Stearns analyst Jeffrey Cianci figures the company may sell its Conoco oil and gas unit to fund investment in its life-sciences division, which includes agricultural biotech and pharmaceutical businesses. Last year, DuPont did deals worth more than \$3 billion to build up life-sciences

operations, and Holliday calls it the company "centerpiece."

GM REVS UP IN MEXICO

GENERAL MOTORS COULD BE facing some angry workers at home—as it makes plans to double production at two Mexican plants. The move comes as GM is getting ready to shut a factory in Flint, Mich. Expanding Mexican output from 300,000 vehicles to 600,000 annually, first reported by Bloomberg, could add thousands of jobs there but could aggravate relations with workers in Flint, where GM plans to close its 2,900-worker Buick City plant. Four GM union locals in Flint voted recently to seek authorization to strike. A GM official says that its trucks and small cars built in Mexico don't replace or compete with the large cars Buick City builds.

HEADLINER: LEONARD ROBERTS

FROM SHACK TO CORNER OFFICE

When Tandy approached Len Roberts five years ago to head its ailing flagship Radio Shack chain, Roberts' initial response was: "I thought Radio Shack died in the 1980s." So did a lot of consumers. But Roberts, a former exec with Arby's and Shoney's, accepted the offer—and has since revived the 6,900-store chain. It still sells batteries, but now it also offers a variety of services, from fixing electronic gadgets to arranging cell-phone and pager connections. Roberts was named Tandy's president in 1996.

Now, Tandy is reward-

ing Roberts, 49, with the top job. On Apr. 6, it announced that Roberts would take over from John Roach, 59, as CEO of the Fort Worth retailer on Jan. 1, 1999. Roach will stay on as Tandy's chairman.



After selling several unsuccessful businesses, \$5.4 billion Tandy is focusing on Radio Shack. Roberts says he plans more expansion through partnerships, such as those with Sprint Spectrum, which sells wireless phones and other products in Radio Shack stores, and PC maker Compaq.

*By Stephanie Anderson
Forest in Dallas*

CLOSING BELL

WRONG NUMBERS

Motorola is making a habit of surprising Wall Street with negative earnings forecasts. On Apr. 6, the day after it released sluggish first-quarter earnings, Motorola spooked investors with predictions of a bleak second quarter due to Asia's crisis and price pressure in cellular products. Shares fell 11%, to 53½. Some analysts are downgrading 1998 earnings estimates more than 20%. "The heat is on to do something radical," says Hambrecht & Quist's Eric Zimits. The stock rebounded slightly, to 54½, on Apr. 8.



MICROSOFT CLICKS ON VENTURE CAPITAL

MICROSOFT IS KNOWN FOR aggressively buying up software startups. Now, it's getting into the venture-capital game, too. The Redmond (Wash.) software giant has invested \$10 million in a new fund raised by Accel Partners. Other corporate investors are Compaq Computer and Lucent Technologies. Jim Breyer, an Accel partner, says the firm's strategy is to align with industry leaders and not just Microsoft.

CONSECO: INSURER AND LENDER BOTH?

IT'S NOT ON THE SAME SCALE as the Citicorp-Travelers megamerger, but in its way, the combination of life and health insurer Consecro with beleaguered subprime lender Green Tree Financial may

be just as radical a move. Unlike the 19 prior acquisitions that Consecro CEO Stephen Hilbert has made in the past 15 years, this one is not about cutting costs. His idea for Green Tree is to cross-sell consumer loans and insurance, a small-scale version of Citigroup's proposed financial-services supermarket. Investors seem to prefer the old Hilbert. The stock dropped 15% on the news. "Why buy the cow when you can buy the milk," asks analyst Ira Zuckerman of Nutmeg Securities. He says Hilbert could have gotten the cross-selling through partnerships without spending close to \$7 billion in stock.

will still be years before consumers buy high-definition TVs in big numbers. No matter, makers of digital broadcast equipment are earning some money right now. At the National Association of Broadcasters meeting in Las Vegas in early April, Sony announced more than \$100 million in orders for high-definition cameras, videotape recorders, and switches. And Harris says it expects to sell more than \$3 billion in digital transmitters, antennas, and encoders over the next six years—doubling its annual sales of communications gear.

ET CETERA...

- Xerox will lay off 9,000 workers and take a \$1 billion charge against earnings.
- Household International and Beneficial sealed a merger worth close to \$8 billion.
- GE's first-quarter earnings rose 13%.

WARMING UP FOR DIGITAL TV

DIGITAL TV HAS BEEN A LONG time coming. This November, 26 stations in major cities will begin broadcasts, but it

McKinsey Andersen BCG Kearney Ernst Price EDS

THEM.

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BY OWEN ULLMANN

BUSINESS VS. THE RIGHTEOUS: WHY TRADE SANCTIONS ARE SOFTENING

Last spring, U.S. plans to punish rogue nations with tougher trade sanctions were sprouting like Washington daffodils. Not anymore. After months of outraged comments by American allies and growing opposition from U.S. business, the Clinton Administration and Congress are quietly backing away from economic behavior modification.

One of the reasons: sanctions fatigue. The use of trade investment bans to pressure tyrants and governments that are guilty of human and religious rights abuses has spread all the way to city councils. Now it's dawning on lawmakers at all levels that righteousness means business and damaged relations with allies and trading partners. Meanwhile, the Clinton Administration—with a wink from Hill leaders—are looking for ways to soften existing sanctions.

WINDING DOWN. The latest example is the quiet easing of the U.S. trade embargo on Cuba. Following a cue from Pope John Paul II—who criticized American sanctions during his January visit to Cuba—the Administration announced on Mar. 20 that it will allow flights into and out of Cuba for humanitarian and family visits and increase annual gifts to island residents up to \$1,200. It also gave preliminary approval for a trade show in Cuba for U.S. makers of medical and pharmaceuticals. That could lead to the first such exhibition in 40 years. The next move: selling food to Cuba and expanding medical sales.

The Administration also plans to ignore provisions of the Helms-Burton Act authorizing Americans to sue in federal court for loss of expropriated property in Cuba. The Clinton Administration has never fully enforced the law, fearing a challenge in the World Trade Organization on grounds that it tries to impose U.S. laws on foreign corporations. In return, the European Union will probably let the mid-April deadline on its WTO complaint against the Helms-Burton Act to lapse. Don't expect the Administration to enforce the penalties

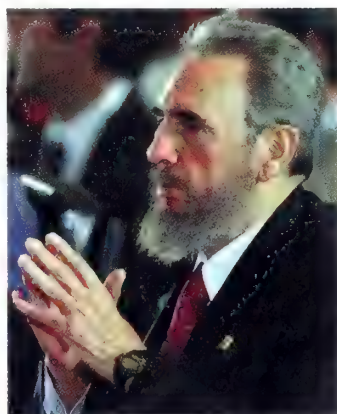
provided in the 1996 Iran-Libya Sanctions Act anytime soon, either. It calls for sanctions against foreign companies that invest more than \$20 million in Iran or Libya. Although President Clinton signed it with great fanfare, he backed down when France's Total, Russia's Gazprom, and Malaysia's Petronas called Washington's bluff with a planned \$2 billion investment in Iran's oil and gas fields. Officially, the White House has been studying the deal for six months while quietly hoping it will collapse. Meantime, the Administration has been holding congressional critics at bay with hopes of a rapprochement with Iran.

Other limits have also been eased. The Administration will not press human rights complaints against China in the U.N. And when the Maryland legislature took up a bill to sanction Nigeria for human rights abuses—just as it once punished South Africa for apartheid—the State Dept. lobbied to kill it.

Other states are feeling pressure to overturn foreign-policy efforts. In Massachusetts, for example, a coalition of more than 500 businesses, the National Foreign Trade Council, is threatening to take the state to federal court over a 1997 law barring companies that do business with Burma from getting state procurement contracts. That has alarmed grassroots activists. "If we tell states they can't assert their own values in government procurement, then we have killed democracy," says the Sierra Club's Daniel Seligman.

Unilateral sanctions will always be a cheap way for lawmakers to express displeasure with other countries. This year, a trade-embargo bill could pass Congress that would punish Sudan for religious persecution. But it exempts the only import that the U.S. wants to buy: gum arabic, used in soft drinks. As business keeps up the pressure, sanctions are increasingly being reduced to such toothless gestures.

By Paul Magnusson, with Gail DeGeorge in Miami



CASTRO: Answered prayers?

CAPITAL WRAPUP

ARMEY'S ASSAULT ON RUBIN

House Majority Leader Dick Armey (Tex.) privately concedes that Clinton Administration scare talk about an Asian financial meltdown has secured House passage this spring of a bill diverting \$18 billion to the International Monetary Fund. A furious Armey, who opposes the measure, grouches at Treasury Secretary Robert E. Rubin raised unwarranted fears that North Korea might invade a weak South Korea. "Rubin's credibility is shot," says an Armey confidant.

PAGING MR. KIM

► How far will House GOP leaders go to pick up a vote? Representative Jay C. Kim (R-Calif.), convicted of campaign-finance abuses, must wear an electronic-monitoring bracelet as part of his sentence—which includes home confinement for two months, with daily office privileges. Trouble is, House rules forbid electronic devices on the floor. No problem, GOP leaders ruled. The ban applies only to "personal office equipment." So Kim can still vote with Newt & Co.

LOCKHEED: NEVER SAY DIE

► Even as it prepares to go to trial, Lockheed Martin clings to the hope of buying Northrop Grumman in a settlement with the Justice Dept. The defense contractor has hired Attorney Robert D. Joffe, a top litigator who has settled antitrust cases such as Time Warner's purchase of Turner Broadcasting. Justice has moved to block the deal in court. But with the Microsoft probe and other mergers preoccupying trustbusters, analysts say Lockheed has a shot.

THEY DON'T WANT TO SAY 'I TOLD YOU SO,' BUT...

What the handful of forecasters who saw a 9000 Dow in '98 see now

In early December, when the Dow Jones industrial average hovered around 8000, the idea that it would breach the 9000 mark by April seemed as likely as Bill Clinton inviting Paula Jones over for dinner. Just look at the '98 forecasts of the investment strategists BUSINESS WEEK consulted then. The consensus of those 45 seers suggested that the market would make only modest gains: a Dow of 8311 at midyear and 8464 at yearend.

Now, just four months later, the Dow has closed once above 9000, and even after a pullback to 8892 by April 8, it still is up 12.43% year-to-date. Other indexes are doing even better. The Standard & Poor's 500-stock index gained 13.52%, and the NASDAQ Composite Index, which had been up over 18% at one point, is still up 15.07%.

Whether the Dow and other indexes can sustain their stunning gains remains to be seen, but one thing is certain: This stock market has come a lot further and a lot faster than almost anyone expected. Anyone, that is, except for a fearless few forecasters, such as Laszlo Birinyi of Birinyi Associates Inc. and Robert J. Froehlich of Scudder Kemper Investments Inc., who, in December, broke away from the crowd and said 1998 would be better for the stock market than most dared to imagine.

BREATHLESS. Birinyi was our most bullish forecaster, looking for 9500 on the Dow by midyear and 10,250 by yearend. Froehlich had slightly lower targets of 9300 and 10,000. Other prognosticators with high targets for the Dow were Eugene E. Peroni Jr. of Janney Montgomery Scott, Anthony F. Dwyer of Ladenburg Thalmann, Joseph Battipaglia of Gruntal, Barry Hyman of Ehrenkrantz King Nussbaum, and Rao Chalasani of EVEREN Securities.

The market has been so strong, even some of these bulls are a little breathless. "I didn't expect the entire year occurring in the first quarter," says Hyman. For now, he is sticking to his original midyear forecast of 9300 and a 4%

to 7% pullback in the second half. But he has been so impressed by the market's momentum that he fully expects the Dow to recover and close the year at 9450 rather than the 9150 he originally estimated. Says Hyman: "The market has the ability to shrug off a lot of bad news."

There's no better example of this than how investors have reacted to a sharp drop in analyst estimates for first-quarter earnings. All winter long, company analysts have been cutting estimates sharply—without much lasting impact on overall stock prices. That doesn't surprise EVEREN's Chalasani. "Investors have been willing to look beyond 1998 earnings and trade on expected 1999 earnings," he says. "That's the kind of behavior you see in a long bull market."

In climbing so far, so fast this year, the market also seems to have downplayed the possibility of serious or lasting damage from Asian economic and financial turmoil. "It looks like the impact will be in the short term, not for the longer term," says Dwyer, the market strategist for Ladenburg Thalmann & Co.

"Last year, everyone was assuming a worst-case scenario from Asia," says



Birinyi, who studies the flow of funds into and out of stocks, not international trade.

But Birinyi looked back to the stock market's reactions to the Mexican financial crises of 1994 and 1982 and determined that the fears were much overblown. "There was so much pessimism," he notes. "In the market, that's a big plus."

Chalasani also believes that the Street misread the Asian crisis. "The result has been lower inflation and greater liquidity [in the financial system], and that leads to higher stock prices," he says. Indeed, most foreign markets, including some in battered Asia, are well into the plus column so far this year.

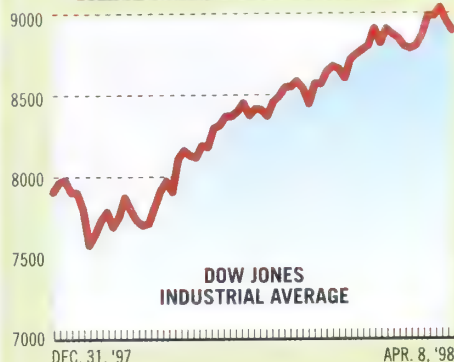
The worries about Asia's impact on the U.S. might have been less if the stock market hadn't been so high for so long. After all, when the seers were peering into 1998, they were looking at a market that had enjoyed an unprecedented three years of 20% or greater gains. Gruntal & Co.'s Battipaglia says the market's recent results have been so much greater than the long-term average of 11% a year that "it's like climbing Mount Everest." People keep expecting to come down the other side, he adds, but this mountain is higher than anyone thought. "The stock market reflects the unprecedented success of the dominant economy in a global marketplace in a time of relative peace," says Battipaglia. "So, financial values deserve to be at these levels and could go higher still."

OPPORTUNITY. Not that the next 1000 points is going to be easy. Sure, climbing from Dow 9000 to 10,000 is only 11.1%. In contrast, it took a 25% gain in stock prices a few years ago to move the Dow from 4000 to 5000. And in the past few years, sharp ascents usually have been followed by months of "sideways action" in which the Dow bounces around within a range of a few hundred points.

But some of our forecasters think the sideways move may tilt downward. Ladenburg Thalmann's Dwyer says he is tempering his enthusiasm for now, because he expects a correction soon. Still, he counsels investors not to fear a correction but to look at it as an opportunity to buy at lower prices. Adds Peroni of Janney Montgomery Scott: "All the fundamentals are very much in place."

Certainly, the mergers-and-acquisitions boom is still gaining steam. Indeed, the megamerger of banking behemoths

REACHING FOR THE SKY



HOW THE REST OF THE MARKET STACKS UP

YEAR-TO-DATE PRICE GAIN*	
DOW JONES INDUSTRIAL AVERAGE	12.43%
S&P 500	13.52
NASDAQ COMPOSITE	15.07
RUSSELL 2000	8.77

*THROUGH APR. 8, '98

DATA: BLOOMBERG FINANCIAL MARKETS

"I didn't expect the entire year occurring in the first quarter"

BARRY HYMAN

Ehrenkrantz King Nussbaum
TOP

"Investors have been willing to look beyond 1998 earnings and trade on expected 1999 earnings"

RAO CHALASANI

EVEREN Securities
CENTER

"There was so much pessimism [about Asia]. In the market, that's a big plus"

LASZLO BIRINYI

Birinyi Associates
BOTTOM

moth Citicorp and brokerage-and-insurance empire Travelers Group Inc., announced on Apr. 6, was the catalyst that finally pushed the Dow over 9000 (page 34). No doubt, the stunning deal will lead to others—and that will energize stock prices once again.

The river of cash heading into the stock market is deep and wide. With mutual funds, cash follows performance returns, and with most funds scoring double-digit yields so far this year, the money is expected to keep rolling in. And Birinyi, whose computer systems track every trade, says investors are making an impact on the market individually as well. There was "tremendous retail investor interest" in Citicorp's stock well before the Travelers deal, and it hasn't closed below 112 all year. Traditionally, individual investors have shied away from high-priced stocks.

Sky-high market valuations can lead to short-term market volatility, notes Scudder Kemper's Froehlich. But, he adds, while the market hasn't experienced these valuations before, neither has it seen 76 million people focusing on retirement investing, a boom in capitalism and consumerism around the world, along with a technological revolution. "The old models that people used to forecast the market don't capture that," says Froehlich. "If they did, a few forecasters would be wrong about the market, and every one else would have been right."

By Jeffrey M. Laderman and Suzanne Woolley in New York

EARNINGS

CORPORATE PROFITS: FADING ... OR STILL VIGOROUS?

How to make sense of conflicting forecasts

When it comes to corporate bottom lines, brokerage-house analysts are perennial optimists. Sure enough, their forecasts for all of 1998 show a 9.2% gain. But for the quarter that just ended, their predictions have been dour—a 0.4% decline in operating earnings for the companies of the Standard & Poor's 500-stock index.

On the other hand, their colleagues, the investment strategists who take a broad view of market trends, are predicting a 6.4% increase for the first quarter—with some expecting double-digit gains. This apparently unbridgeable difference of opinion is omnipresent in the financial press, and investors are confused. Is this a routine squabble among market seers—or is something deeper at work?

In fact, this clash of crystal balls could have powerful implications for investors. With analysts, who track companies, so negative, it could well mean that a substantial amount of bad news is already reflected in stock prices. But with strategists predicting continued low interest rates and steady growth—the basis of their glowing forecasts—there is the promise that first-quarter earnings surprises, when they come, are likely to be positive.

RATCHETING DOWN. One reason for the dichotomy is that analysts have been ratcheting down their estimates all quarter as individual companies warned that earnings would come in below analysts' expectations. At the beginning of the year, analysts were expecting 9.6% growth in the first quarter, according to I/B/E/S International Inc. Strategists, in contrast, typically do not react much to individual companies' earnings pre-announcements, focusing instead on the overall economy—the big picture.

Analysts and strategists alike are more optimistic about gains in total net earnings than in operating earnings, because they expect companies to report fewer nonrecurring losses

from restructuring during 1998. "That has certainly been a source of major confusion," says Dan Laufenberg, chief U.S. economist for American Express Financial Advisors.

Another source of confusion is the change in the calculation for earnings per share by the Financial Accounting Standards Board in the last quarter of

1997. The new rules require some companies to include more potential dilution (caused mainly by the use of stock options) when calculating earnings per share. Some companies haven't restated their numbers from the first quarter of 1997, which makes their earnings growth numbers a bit suspect.

Earnings forecasts also have been complicated by geopolitical forces and unusual weather patterns—the El Niño effect—along with dramatic declines in oil prices. Asian perils have obscured the picture further. As a result, earnings gains vary widely from industry to industry (table). Big energy users, such as manufacturing and transportation companies, have benefited from declines in oil prices, while oil companies, understandably, are taking hits to earnings. "There is a split this quarter between industries that is really dramatic," says Ed Keon, an earnings analyst at I/B/E/S International.

UNUSUAL DIVERGENCE.

The contrast in earnings is stark. Of the 75 industry groups that make up the S&P 500, 29 are expected to grow at more than 19%, while 19 are expected to show declines. It's unusual to have a lot of industries expecting drops and a lot expecting fast growth, notes Keon.

In examining industry and individual company numbers alike, operating earnings are the most reliable indicator of corporate health. By stripping out all one-time charges, analysts say they can get a better picture of a corporation's earnings trend. "Operating results are more reflective of the financial viability of the company," explains Gabriel Napolitano of Goldman, Sachs & Co. Reported numbers tend to be much more volatile, she says, adding "it is very difficult to derive a normalized earnings growth rate." That's what earnings from continuing operations delivers.

However, investors shouldn't neglect looking at the bottom-line earnings as well, since operating earnings are also a way for a company to brush unpleasant events under the rug. A comparison of operating and reported earnings is the best way to get the whole story, particularly in an earnings season with such conflicting outlook. Investment strategists may well win the day with the rosier outlook, but that will be small solace for investors who fail to sort out all the forces that affect earnings.

By Amey Stone in New York



Industry Earnings: All Over the Map

INDUSTRY GROUP	ESTIMATED GROWTH RATE	
	1ST QUARTER 1998	FULL YEAR
OIL	-27%	-3%
SEMICONDUCTORS	-21%	-3%
COMPUTER MANUFACTURERS	-3%	13%
FOREST PRODUCTS	118%	90%
TRUCKING	20%	25%
AIRLINES	14%	10%
SOFTWARE	37%	43%
HOMEBUILDERS	44%	27%
S&P 500		
ANALYSTS	-0.4%	9.2%
STRATEGISTS	6.4%	7.8%

DATA: I/B/E/S INTERNATIONAL



DOES YOUR COMPANY HAVE AN IDEA WE CAN TAKE SOMEPLACE?

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GTE
PEOPLE
MOVING
IDEAS

BY GENE G. MARCIAL

ALCOA FORGES STRONG LINKS

Metals have yet to shine in this raging bull market, but investment manager Ed Wachenheim III is counting on one producer to score big: Aluminum Co. of America (AA). "The Street has ignored Alcoa because it's misperceived as just a plain cyclical stock," says the

CEO of Greenhaven Associates, a New York investment firm that has accumulated 1.3 million shares of the largest aluminum producer.

The stock has been lackluster, skidding from 89 last summer to 68 on Apr. 7. But Wachenheim says he finds it exciting. What gives?

"In reality, Alcoa could be regarded as a growth stock—it has many of the characteristics of a high-quality growth company," he explains. And yet its shares trade at a price "typical of a low-quality cyclical company whose earnings are cyclically weak," he says.

Here's why Alcoa deserves more respect: It produces large cash flows even when aluminum prices are soft. Last year, prices were weak, yet Alcoa's cash flow from operations rose to \$1.8 billion, or \$11 a share, from \$1.2 billion, or \$7.35, in 1996.

That has enabled Alcoa, Wachenheim notes, to buy assets at bargain prices. Recently, Alcoa paid \$410 million for Inespal, a Spanish aluminum producer formerly government-owned. Inespal's replacement value: \$2.5 billion.

Alcoa also has agreed to acquire No. 3 Alumax, creating a company with \$17 billion in annual revenues and aluminum output of nearly 4 million tons. Alcoa projects revenues will climb an average 15% a year, from \$13 billion in 1997 to \$20 billion by 2000.

Wachenheim is also impressed with Alcoa's earnings: In 1997—with ingot prices in London averaging only 73¢ a ton—Alcoa posted diluted earnings of \$4.62 a share. This year, assuming ingot prices stay at 65¢ to 70¢ a ton, he esti-

mates earnings will rise to \$5.50. But next year, with Inespal and Alumax earnings kicking in, he sees profits jumping to \$1.8 billion to \$1.9 billion, or \$10.50 to \$11 a share, based on ingot prices of 85¢ a ton. He says Alcoa deserves a price-earnings ratio of 12 to 13, or a price of 125 to 140 a share.

DON'T CROSS OFF CROSS

Since 1952, when A. T. Cross (ATX.A) introduced its gold-plated ballpoint pen now synonymous with the Cross name, the product had been a huge success—until 1995, when sales peaked. And after hitting a high of 41 in mid-1996, its stock has since slid downhill, closing at 10¢ on Apr. 7. Earnings have followed suit, falling from 80¢ in 1995 to 40¢ in 1996 and a loss of 26¢ in 1997. End of the line for Cross?

Value investor Mark Boyar thinks not. He says Cross is one of the best bargains around, so has accumulated a big stake. Two factors whet his appetite. Cross has launched new computing products, including CrossPad—with IBM as its partner. The CrossPad, designed by Cross and IBM, transforms how users store, organize, and share notes by writing in ink on a pad and unloading the handwriting directly to a PC.

And there is a buyout angle: With the family of Chairman Bradford Boss and CEO Russell Boss owning 100% of Cross Class B stock, which elects two-thirds of the board, a friendly buyout could be easy to achieve—if a serious suitor comes along. "There are no buyout rumors, and the family claims no interest in selling," notes

Boyar. But the family might be enticed by a tax-free stock deal, he argues, with the likes of Fortune Brands, formerly called American Brands before it got out of the tobacco business. With its famous name in pens and new computing products, Cross could be a compelling acquisition for Fortune, a global consumer products company, says Boyar.

Given its "solid consumer franchise, a

strong balance sheet, significant cash flow-generating abilities, and new computer products," says Boyar, Cross has an intrinsic value of 28 a share. A Fortune spokesman wouldn't go beyond saying the company continues to look for acquisitions. Cross CFO John Rugieri says the company is investing heavily in new products to turn around. Cross, he adds, is not for sale.

RICH HARVEST AT PIONEER?

The seed business, an unlikely takeover area, may be the next scene for just that. A stock that some major market players have been eyeing, both for its long-term fundamentals and its takeover allure, is Pioneer Hi-Bred International (PHB), the nation's largest producer of corn seed and a leading soybean seed producer, whose shares hit a 52-week high of 111½ on Mar. 12, up from 98 in late January. It has since eased to 100 on profit-taking.

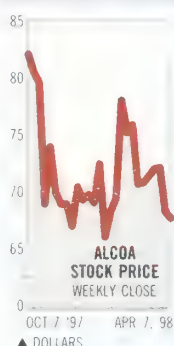
What's the reasoning behind the takeover theory? For one thing, DuPont already has acquired a 20% stake in Pioneer, investing \$1.7 billion, or about \$104 a share, for a research alliance and a joint venture to develop new crops of value to farmers, livestock producers, and consumers. Another seed company, Dekalb Genetics, has put itself up for sale. Monsanto, Dow Chemical, and Cargil are reported to be potential bidders.

Stephen Leeb, editor of *Persona Finance*, says Pioneer in a buyout could easily command \$150 a share. But the stock could hit 150 in a year just based on long-term value, he says.

Over the past five years, Pioneer's profits have grown nearly 20% a year as unit sales and profit margins rose with higher grain demand, says Leeb.

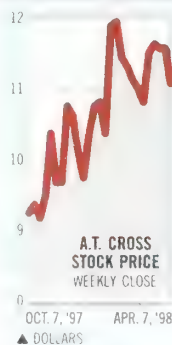
Pioneer also has a partnership with Genome Sciences for DNA sequencing—which has the potential for a breakthrough in corn yields. Leeb sees Pioneer earning \$3.55 a share this year and \$4.20 next, up from 1997's \$2.95.

AN UNALLOYED BARGAIN



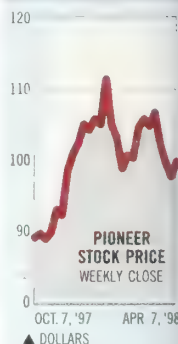
DATA: BLOOMBERG FINANCIAL MARKETS

IS THE WRITING ON THE WALL?



DATA: BLOOMBERG FINANCIAL MARKETS

SEEDS TO SOW



DATA: BLOOMBERG FINANCIAL MARKETS



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JAPAN

BAGGING MORE TIGERS

Japan sees opportunity in Asia's crisis

Construction equipment maker Bangkok Komatsu Co. looked like a goner. After Thailand's baht crashed last year, local contractors stopped their projects and canceled orders for Komatsu's land excavators. With 70 unsold machines worth roughly \$70,000 each piled up in its stockyard and warehouse, the Japanese-Thai joint venture sent 80 out of 140 workers home and shut down its factory on the outskirts of Bangkok.

That was in December. This month, Bangkok Komatsu will be back in business. But it will no longer sell equipment locally. Instead, assembly lines retooled at minimal cost will churn out hundreds of excavators for the U.S. market. "This has been a very good shock for us," says Nobutsu Ohira, vice-president of Bangkok Komatsu. "We are setting tougher targets in terms of quality and cost."

Such stories illustrate how Japanese

companies hope to survive and perhaps emerge stronger from Asia's economic crisis. With billions of dollars already invested in Southeast Asia, Japanese companies are not pulling out of the region. Instead, they are digging in deeper, buying bigger shares of cash-strapped venture partners, and ramping up exports to the rest of the world.

RACE TO RETOOL. The result could be a major change in global trade flows. Japanese-controlled plants in Southeast Asia already export \$70 billion in goods out of the region. If they expand that capacity dramatically, U.S. imports could surge and some American manufacturers could find themselves under pressure.

Already, one out of three products manufactured in Southeast Asia—from glass to computer parts to VCRs—come from a Japanese subsidiary or joint venture. Japanese companies invested \$10 billion in South Korea, Thailand, Malaysia, Indonesia, and the Philippines combined in 1997. That compares with just \$7.4 billion invested by U.S. companies, according to the Japan External Trade Organization. After the current crisis began last July, Japanese investment shifted from building new factories to retooling or expanding existing

"This is an opportunity," says Aki-Seki, a deputy executive officer in charge of corporate strategy at Denso Corp., which is buying out partners' shares in Indonesia and Thailand. "We do not intend to stop investing," he says.

Although many companies are taking a wait-and-see attitude before opening new factories, total Japanese investment this year is expected to be the same or drop only slightly. "I think they will at least maintain the current state of investment," says Japan's chief economic adviser in Bangkok, Chawakrengkai.

The crisis has wiped out local demand for Japanese products and forced companies into focus. "In order for Japanese companies not to go bankrupt in Southeast Asia, they have to expand exports a lot," says Daisuke Hiki of the Institute of Developing Economies in Tokyo. The volume of exports from revamped Japanese operations in Southeast Asia could soar this year once the retooled factories are running, Hiratsuka says.

PT CARS. Japan's battered automotive industry cannot absorb all these exports. That means 60% of them will go to the booming economy of the United States and the remaining 40% will go to Europe, Hiratsuka says. Shock-absorber maker Tokico, which used to supply local car body factories in Thailand. Now exports 62,000 shock absorbers to the U.S. every month. Matsushita Precision Industrial Co. of Japan made 40% more color TVs this year, many of them U.S.-bound. There are exceptions to this trend as well. Japanese carmakers, who had targeted the Southeast Asian middle class, Honda and Toyota cannot rely on export because they already have big operations in the U.S. and Europe. Daihatsu and Mitsubishi have closed assembly lines.

Other manufacturers were export-oriented in the first place. Ball-bearing maker Minebea has invested \$148 million in overseas facilities last year, much of which went to Thailand. In Malaysia, synthetic fiber maker Toray Industries Inc. plans to invest \$265 million to expand its production to include polyester film and rayon. Electric Glass Co. will invest \$100 million in a new glass-fiber factory in Singapore. Computer giant NEC Corp. will sink \$185 million into a new semiconductor test and assembly facility in the Philippines, NEC is putting \$100 million into a new electronics com-

Computer giant NEC is opening a new factory in the Philippines, and it will sink \$185 million into a new chip facility in Singapore

ponents factory with 750 workers. Both NEC and Fujitsu Ltd. may open hard-drive factories there soon. "It's like the gold rush of 1849 in the United States," crows Hideaki Kobuna, president of NEC Components Philippines, which makes printed circuit boards outside Manila. "The Philippines is just taking off."

Some of this expansion will affect Japanese-owned assembly lines elsewhere. Japan's largest aluminum processor, Showa Aluminum Corp., will shut down an assembly line this fall in Japan while doubling production to more than 100,000 refrigerator parts per month in the Philippines. "Now that the peso is so weak, it makes more sense to pro-

duce here," says Keisuke Furuhashi, a financial manager at Asahi Tec. "In the U.S., we have been in the red for 10 years."

Furuhashi, like other Japanese managers, sees the crisis as a chance to assert more control over Asian operations. Thailand's Board of Investment so far has approved 40 of 125 applications made by Japanese companies to take larger stakes in their joint ventures. Honda Motor Co. invested \$102 million in March to bail out its cash-strapped Thai partners and acquire most of its car-assembly joint venture. Toyota, Nissan, and Mazda may follow suit. While the Thais are reluctant to give up control, "essentially they've got no choice," says Robert McMillen, of Seamco Securities in Bangkok.

Despite all the activity in Southeast Asia, Japanese companies have made few moves in South Korea, where anti-Japanese sentiment prevails, or Indonesia, where the value of the local rupiah fluctuates wildly. Yet there is some movement on those fronts as well. Sumitomo Chemical Co. bought \$33.5 million in shares from a beleaguered partner in February to boost its stake in Korea's Dongwoo Pure Chemical from 40% to 90%. Tanabe Chemical Industry plans to build a new plant in Indonesia that will produce 50 tons a month of industrial paint. Debt-plagued Fuji Bank boosted its stake in an Indonesian leasing venture from 50% to 80%.

Japanese companies are doing this because they believe Asia will rebound, and they want to be there when local customers spend once more. In the process, they may end up with more control over companies in the region than ever. Even in crisis, industrial Japan maneuvers for advantage.

By Emily Thornton in Tokyo, with Ron Corben in Bangkok, Hugh Filman in Manila, and Moon Ihwan in Seoul

HOW JAPAN IS DIGGING INTO SOUTHEAST ASIA

BUYOUTS

Japanese companies are buying bigger stakes in cash-strapped local partners throughout the region.

EXPANSIONS

Export-oriented companies are expanding production in Asia. At the same time, they are shutting down assembly lines in Japan and pulling out of unprofitable ventures in the U.S.

EXPORT BLITZ

Taking advantage of Asia's weak currencies, Japanese companies will boost the volume of exports of such products as car parts and electronics from Southeast Asia by about 30% this year.

DATA: BUSINESS WEEK

duce these parts more cheaply in the Philippines than in Japan," explains Shunji Umemura, a business-planning manager for Showa Aluminum.

Car-parts maker Asahi Tec Corp. pulled out of its American joint venture the same day it decided to increase its stake in two Thai joint ventures. "With a greater



EDITED BY JOHN TEMPLEMAN

HONG KONG: NOW THE RULE OF LAW IS IN JEOPARDY

It's already quite a ritual. Hong Kong Chief Executive Tung Chee Hwa proposes an unpopular change in the law. Pro-China legislators, installed last year by Beijing in place of its vocal critics, dutifully rubber-stamp the idea. So it was no surprise when, on Apr. 7, lawmakers turned a deaf ear to legal experts, newspaper editorialists, and democracy advocates, and approved Tung's move to exempt Chinese government agencies from local laws.

Tung's gesture is just his latest kowtow to Hong Kong's new overlords. In March, he decided not to prosecute China's Xinhua News Agency for violating the privacy law. He didn't press fraud charges against an influential pro-China businesswoman. Tung's moves are stoking fears that some parties are more equal than others in the new Hong Kong, despite China's repeated pledges to keep the former colony's evenhanded legal system. "It makes me cringe," says Audrey Eu, who chairs the Hong Kong Bar Assn.

EASY DODGE. Defenders of Tung insist the criticism is overblown. He is, they say, simply updating colonial laws that gave exemption to the British Crown. But there's a big difference. The Chinese government has many more direct business interests in Hong Kong than the British ever did. From red chips such as Citic Pacific Ltd., part-owned by the central government, to companies run by the People's Liberation Army, every arm of China's government has its business tentacles in Hong Kong.

State entities involved in commercial operations are supposedly still subject to Hong Kong laws. But companies could easily dodge that proviso by forming subsidiaries that claim to be state agencies. "Once we accept this, it might open a whole box of strange creatures," warns Law Yuk Kai, director of Hong Kong Human Rights Monitor.

Already, Xinhua has run rings around one Hong Kong le-

gal safeguard. Last year, firebrand pro-democracy politician Emily Lau requested to see its file on her. Xinhua dragged its heels for 10 months, way beyond the law's 40-day deadline, then curtly and unconvincingly replied that it had no such file. Tung shrugged off the violation as "technical."

Such a cavalier attitude toward breaches of Hong Kong laws are starting to rattle foreign and local businesses alike. A Hong Kong property developer, for example, alleges that a Xinhua subsidiary backed out of a contract after the stock market crashed last fall. The developer has filed suit, but Xinhua now denies any involvement in the deal. And it's not just local companies that may have to contend with a privileged opponent: America Online Inc., for instance, has a new partnership with a Xinhua-backed company to bring an Internet access provider to Hong Kong.

In his eagerness to please Beijing, Tung is making it harder for the local economy to recover from the Asian crisis. Instead of reassuring investors about Hong Kong's legal system, he risks scaring them off by putting the rule of law in question. "Hong Kong is doing [China] no favor in not trying to enforce its own rules," says Michael E. H-

Golyer, a political economist at Hong Kong Baptist University.

Fears about the rule of law are eroding Tung's support among ordinary Hong Kongers, too. Recent polls show that only half are satisfied with his government, down from 64% last June. But however unhappy the voters get, byzantine election laws ensure that Beijing's critics will remain a small minority in the new Legislative Council to be elected in May 24. Opponents may have few voices in the legislature, but they will be shouting and screaming when the new legislature begins one of its first tasks: drafting laws to define and ban subversive activities.

By Bruce Einhorn in Hong Kong



TUNG: Kowtowing to Beijing

GLOBAL WRAPUP

PHILIPPINE ELECTION WORRIES

► Philippine business leaders worry that Vice-President Joseph E. Estrada won't be able to lead the country out of its economic crisis if he wins the May 11 presidential election. For one thing, he is close to several leading cronies of the late dictator Ferdinand Marcos. Polls indicate that the former tough-guy movie actor may get 28% of votes—twice as much as his nearest rivals such as business' favorite, House of Representatives Speaker Jose C. de Venecia Jr.

The speaker is supported by President Fidel V. Ramos. But even with the full backing of Ramos's substantial party machine, it will be hard to close the gap with Estrada. Former First Lady Imelda Marcos, one of the 11 candidates, has only marginal support.

KOREAN TALKS RESUME

► Talks between North and South Korea on Apr. 11 in Beijing could mark the first step in a long thaw between the divided countries. But Korea watchers do not expect any early breakthrough toward détente.

Seoul wants to enable visits between families divided since the end of the Korean War in 1953 and arrange for the exchange of special envoys. In return, it is ready to supply 200,000 tons of fertilizer over time.

Pyeongyang insisted on holding the talks, the first government contacts since President Kim Il Sung died in 1994, in a third country and not on the world's last cold war border at Panmunjom. It is also sticking to its position that it only will make a peace arrangement on the Korean peninsula directly and exclusively with the U.S.

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EXECUTIVES

Stock options plus a bull market made a mockery of

For Richard M. Scrushy, CEO of health-care company Healthsouth Corp. in Birmingham, Ala., 1997 was an outstanding year. He took home \$106.8 million in salary, bonus, and—primarily—exercised options

to become the third-best-paid CEO in BUSINESS WEEK's annual executive pay survey. While his compensation may boggle the mind, so has his performance. In the 14 years since he founded Healthsouth with three partners and \$50,000, Scrushy has built it into the largest outpatient care center in the U.S., with a market capitalization of \$11.4 billion. In 1997, the stock rose 31%, bringing its gain over the past 10 years to more than 1,200%. Says Scrushy: "Finally, I rang the bell and got paid."

So did Ray R. Irani, longtime CEO of Occidental Petroleum Corp. In order to replace an incredibly lucrative 1990 employment contract that provided Irani a guaranteed paycheck worth close to \$5 million a year for life, Occidental's board gave him a 1997 payoff valued at \$101.5 million. That was enough to make Irani one of the best-paid executives in Corporate America. Did Irani, too, build a business from scratch, or bring shareholders great rewards? Hardly. Since 1990, Occidental's stock has risen just 10%, and the company lost \$390 million in 1997—in part, due to Irani's sweet deal. Occidental is being sued by Teachers' Retirement System of Louisiana for breach of fiduciary duty. Irani wouldn't comment.

REALITY CHECK. If these two examples leave you scratching your head, you're not alone. While the concept of linking pay to performance has caught fire in the boardroom, reality has proved to be quite different. Certainly, many CEOs who delivered the goods last year received huge—and often

justifiable—payoffs. And a very few poorly performing executives saw a portion of their pay docked. But the proliferation of stock options, grants, combined with the rise of cushy retirement deals, sign-on bonuses, and ironclad severance packages for CEOs, have made a mockery out of many attempts to truly link pay to performance.

The upshot: Good, bad, or indifferent, virtually

THE TOP

		1997 SALARY AND BONUS THOUSANDS OF DOLLARS	LONG-TERM COMPENSATION	
1	SANFORD WEILL TRAVELERS GROUP	\$7,453	\$223,272	\$23
2	ROBERTO GOIZUETA COCA-COLA	4,052	107,781	1
3	RICHARD SCRUSHY HEALTHSOUTH	13,399	93,391	16
4	RAY IRANI OCCIDENTAL PETROLEUM	3,849	97,657	10
5	EUGENE ISENBERG NABORS INDUSTRIES	1,675	82,872	8
6	JOSEPH COSTELLO CADENCE DESIGN SYSTEMS	584	66,258	6
7	ANDREW GROVE INTEL	3,255	48,958	5
8	CHARLES McCALL HBO & CO.	1,725	49,684	7
9	PHILIP PURCELL MORGAN STANLEY DEAN WITTER	11,274	39,533	9
10	ROBERT SHAPIRO MONSANTO	1,834	47,491	4

AND TEN

		1997 SALARY AND BONUS THOUSANDS OF DOLLARS	LONG-TERM COMPENSATION	
1	JAMES CROWE* WORLDCOM	\$151	\$68,913	\$0
2	ANTHONY PETRELLO NABORS INDUSTRIES	575	47,722	3
3	JAMES DIMON TRAVELERS GROUP	5,255	39,005	7
4	LAWRENCE LASSER MARSH & MCLENNAN	12,870	24,585	8
5	J. CARTER BAGOT BANK OF NEW YORK	8,302	23,193	6

*FORMER CEO OF MFS COMMUNICATIONS

DATA: EXECUCOMP BY STANDARD & POOR'S

WE PAY

any attempts to link pay to performance

one who spent time in the corner office of a public company in 1997 saw his or her net worth rise by at least several million. Thanks to the exploding stock market, CEOs were more handsomely rewarded than ever before. Indeed, the average boss collected an options-fueled package worth \$7.8 million for 1997, pulling down a 35% increase over 1996's \$5.8 million. But for many CEOs,

those gains bore little relation to how well their companies—or investors—did. In the pay-for-performance sweepstakes, the “performance” half of the equation increasingly fell by the wayside.

Big, big money was only the most obvious finding of BUSINESS WEEK's 48th annual Executive Pay Scoreboard. Compiled with Standard & Poor's Compustat, a division of The McGraw-Hill Companies,

the survey examines the pay of the highest-paid executives at 365 of the country's largest companies. The average salary and bonus actually fell, to \$2.2 million from \$2.3 million, as some CEOs deferred bonuses or took options instead.

But don't let that decline fool you. It's just that the upfront elements of pay are shrinking in importance. The real money now comes from the exercise of options, long-term incentive plans, and perks. “Salary and bonus don't mean anything anymore,” says David M. Leach, executive vice-president at pay consultant Compensation Resource Group Inc. Throw in all the extra goodies, and CEOs continue to rake it in. Indeed, although the 35% increase in CEO pay was less than 1996's 54% leap, that's still more than 13 times the average 2.6% raise earned by blue-collar workers and over nine times the 3.8% boost white-collar workers pocketed, according to the Bureau of Labor Statistics' Employment Cost Index. For the year, the average boss earned 326 times what a factory worker did.

Few would dispute that 1997 was a fabulous year for much of Corporate America—and most CEOs weren't shy about taking credit along with the check. The high payouts, they say, were well deserved: Profits rose 5%, and the Standard & Poor's 500-stock index ran up a scorching 31% gain. With

EXECUTIVES

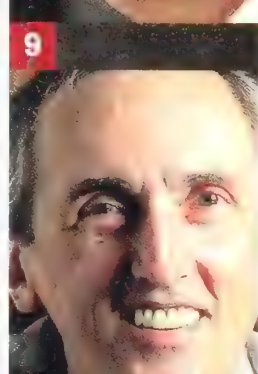
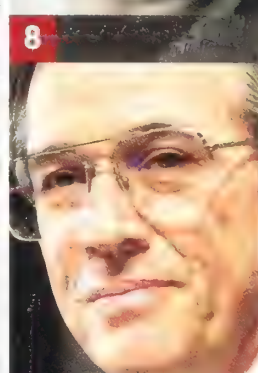
	1997 SALARY AND BONUS THOUSANDS OF DOLLARS	LONG-TERM COMPENSATION	TOTAL PAY
WELCH	\$8,069	\$31,825	\$39,894
GENERAL ELECTRIC			
EY GOLUB	3,469	29,989	33,457
AMERICAN EXPRESS			
AM SCHOEN	1,041	29,905	30,945
AMER. MGMT. ASSOCIATES			
LES HEIMBOLD	2,803	26,409	29,211
TOL-MYERS SQUIBB			
LESH MENTA	2,066	26,298	28,365
INDIAN FINANCIAL			
ENCE BOSSIDDY	5,155	23,082	28,237
EDSIGNAL			
AM STEERE	3,880	24,240	28,120
ER			
WEN CASE	271	26,642	26,913
ERICA ONLINE			
ERT LIPP	3,730	22,570	26,301
ELERS PROPERTY CASUALTY			
EN MARK	3,847	21,544	25,390
ATE-PALMOLIVE			

CEOs

	1997 SALARY AND BONUS THOUSANDS OF DOLLARS	LONG-TERM COMPENSATION	TOTAL PAY
SILVERMAN †	\$ 61	\$27,058	\$27,119
ANT			
ES CAWLEY	4,623	22,461	27,084
IS SCHNEIDER			
AN STANLEY DEAN WITTER	2,460	21,242	23,702
FRESCO	3,700	19,064	22,764
AL ELECTRIC			
CAMERON	2,116	18,897	21,013
ANCORP			

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† BECAME CEO 12/97



Pay For Performance: Who Measures Up... And Who Doesn't

To see how pay matches up to performance, BUSINESS WEEK uses two measurement systems. One relates to how good a job the boss did for shareholders. The other compares what the boss made with how well the company did.

EXECUTIVES WHO GAVE SHAREHOLDERS THE MOST FOR THEIR PAY...

1995-97		Total pay* Thousands of dollars	Shareholder return**	Relative index
1	JAMES SINEGAL Costco	\$1,256	247%	276
2	WILLIAM GATES Microsoft	1,570	323	269
3	B. THOMAS GOLISANO Paychex	1,678	331	257
4	RONALD DOLLENS Guidant	3,052	682	256
5	WARREN BUFFETT Berkshire Hathaway	889	125	254

EXECUTIVES WHOSE COMPANIES DID THE BEST RELATIVE TO THEIR PAY...

1995-97		Total pay* Thousands of dollars	Avg. return on equity	Relative index
1	WILLIAM GATES Microsoft	\$1,570	31%	17
2	DANIEL MIGLIO Southern New England Tel.	2,388	41	1
3	B. THOMAS GOLISANO Paychex	1,678	29	9
4	MARK WILLES Times Mirror	9,388	42	9
5	JAMES SINEGAL Costco	1,256	14	8

...AND THOSE WHO GAVE SHAREHOLDERS THE LEAST

1	LAWRENCE COSS Green Tree Financial	179,291	77	1.0
2	SANFORD WEILL Travelers Group	374,722	422	1.4
3	RAY IRANI Occidental Petroleum	114,557	72	1.5
4	ROBERTO GOIZUETA Coca-Cola	140,812	168	1.9
5	RICHARD SCRUSHY Healthsouth	141,773	205	2.1

...AND THOSE WHOSE COMPANIES DID THE WORST

1	WILLIAM SMITHBURG Quaker Oats	5,158	-106	-39
2	PETER KANN Dow Jones	4,232	-26	-15
3	JAMES ROBBINS Cox Communications	4,092	-1	-
4	STANLEY GOLDSTEIN CVS	7,383	-6	-
5	JOHN BRYAN Sara Lee	15,319	5	-

*Salary, bonus, and long-term compensation paid for the entire three-year period **Stock price at the end of 1997, plus dividends reinvested for three years, divided by stock price at the end of 1995

†As reported by the company in its proxy. May be restated in 1999

DATA: STANDARD & POOR'S COMPUSTAT

stock options responsible for 55% of a CEO's average pay package these days, Wall Street's bulls powered most of the rise.

But those big market gains—along with a huge increase in the number of options granted—have combined to fuel an unprecedented inflationary spiral in executive pay. Take the \$7.8 million paycheck CEOs earned on average in 1997. Just 10 years ago, that would have shot an executive into the No. 13 slot on BUSINESS WEEK's pay rankings; 20 years ago, it would have topped the list.

What's more, the 1997 numbers don't even reflect the largest single option sale ever: In December, Walt Disney CEO Michael D. Eisner exercised 7.3 million options worth over \$400 million. Eisner's move came after the close of Disney's fiscal 1997 year. "Pay just goes up and up and up," says Corey Rosen, executive director of the National Center for Employee Ownership.

So what does it now take to be king of the pay hill? For 1997, Sanford I. Weill, CEO of Travelers Group Inc., was Corporate America's best-paid executive. Thanks to an outstanding year—as well as a controversial technique known as reload options—his total pay package hit a stunning \$230.7 million. His closest competitor, former Coca-Cola Co. CEO Roberto C. Goizueta, cashed in options worth \$104 million before his October death. Others atop the list include Scrushy, Irani, and Eugene M. Isenberg, CEO of Nabors Industries Inc., a \$1.1 billion oil-well drilling company. He took home \$84.5 million in 1997, mostly from exercising 10-year-old options. The payout "doesn't one iota affect the way we work," says Isenberg, whose salary and bonus haven't changed in a decade. Nabors' investors, who have seen shares rise an average of 43% annually over that time, have profited, too.

Indeed, in a year when shareholders saw their own coffers expanded comfortably, many were less likely to complain. Says Robert L. Rodriguez, chief investment adviser at First Pacific Advisors Inc., a \$4.5 billion money man-

ager: "We're not opposed to having people make lots of money if we make lots of money."

Much of the outrage that accompanied news of huge executive pay hikes just a few years ago also seems to have gone into hibernation. "I don't hear the same level of anxiety we heard in the past two years," says Patrick S. McGurn, corporate programs director at Institutional Shareholder Services, a proxy-advisory service. The healthy economy and job market help, as does the fact that employees are participating in the equity market themselves via 401(k) plans or broad-based option plans. According to a study by consultant William F. Mercer Inc., some 30% of the largest 350 companies have set aside grants for broad-based option plans, though only 1% have given them to 50% or more of their employees.

OUTRAGE FATIGUE. Some also think it's because the sums are too huge to comprehend. For example, Henry R. Silverman, CEO of Cendant Corp., is sitting on close to \$1 billion in exercisable stock options (table, page 68). "Since companies are doing well," says governance expert Ira M. Millstein, a senior partner at law firm Weil, Gotshal & Manges, "people aren't focusing on the increasing distance between the top and the bottom or the levels to which CEO pay has gone."

Still, if the dissenting voices have gotten quieter, they haven't disappeared. Options repricing—exchanging options for new options at a lower price after the stock falls—is one area in which activism is rising. The State of Wisconsin Investment Board (SWIB) has made repricing its focus this year, trying to get 22 companies to allow shareholder approval of any such plan. Says a SWIB spokesman: "You don't see this until you see the company's proxy. We think it is an issue that shareholders should have a say in."

The attack on repricing may represent a tactical shift by investors. Rather than decry the swelling level of pay in general, critics are focusing on more specific issues. The AFL-CIO is turning the spotlight on how close ties between execs and directors can lead to excessive pay, for example. And on Mar. 31, the Council of In-

"Salary
and bonus
don't mean
anything
anymore"

THE GOOD, THE BAD, THE UGLY OF CEO SALARIES

Shoppers in the cavernous Costco warehouse stores often bag a bargain. The same goes for shareholders in Costco Cos. By Corporate America's standards, Chief Executive James D. Sinegal comes cheap. His salary has held steady at mere \$300,000 for each of the past three years. His 1997 bonus, at \$200,000, was relative chump change. And over the last three years, he has exercised none of his 48,400 options. Meanwhile, Costco's stock price more than tripled from 1995 through 1997.

The combination explains why Sinegal is one of this year's two pay-or-performance champs, according to BUSINESS WEEK analysis. He gave shareholders the highest return—stock appreciation plus dividends—relative to his compensation. Using another yardstick, which compares a CEO's compensation to the company's return on equity, a core measure of profitability, the leader is the *Übermensch* of software, Microsoft's William H. Gates III (table).

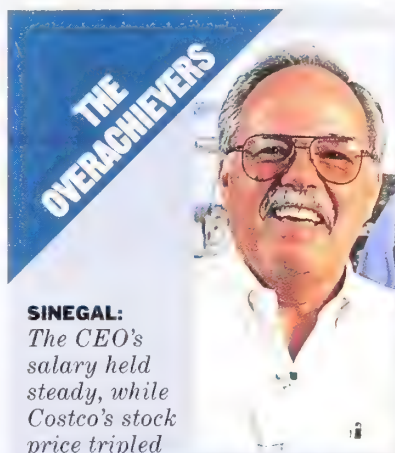
Sinegal's achievements in big-box

retailing are notable. His chain has handily outpaced Sam's Club, the discount-warehouse arm of mighty Wal-Mart Stores Inc. Sam's sales per outlet are only half Costco's. From 1995 to 1997, Costco's shareholder return rose 247%. Sinegal's success formula? The bargain king has a mania about keeping costs down. Costco does no advertising, for instance. And the rapidly expanding retailer now boasts 16 million dues-paying members.

NET PAY. Under Gates, Microsoft has been a growth dynamo, with profits surging 57% in 1997. ROE since 1995 has averaged a muscular 31%. Gates has also made good on his pledge to catch up in Internet services, succeeding so well he has attracted the Justice Dept.'s antitrust scrutiny. Yet Gates's pay is downright parsimonious. Since 1995, Gates has collected just \$1.5 million in total pay. His reward comes via stock ownership: His 22.3% stake is now worth \$47.8 billion.

Which brings us to the less admirable end of our roster. In comparing shareholder returns with pay, investors got the least from Green Tree Financial Corp. Chairman Lawrence M. Coss, who has pocketed a breathtaking \$179 million since 1995, much of it in company shares. All was well until last November, when the company's ever soaring earnings ran into a big problem. Hordes of borrowers had repaid their loans to take advantage of lower interest rates. The stock, which was almost at 50, had lost half its value by yearend. Green Tree ended up booking a loss for 1997's fourth quarter and restating 1996's final period to show red ink. For 1995 through 1997, shareholder return was 77%—far less than it would have been without the blow-up, and minuscule in light of Coss's outsize payout.

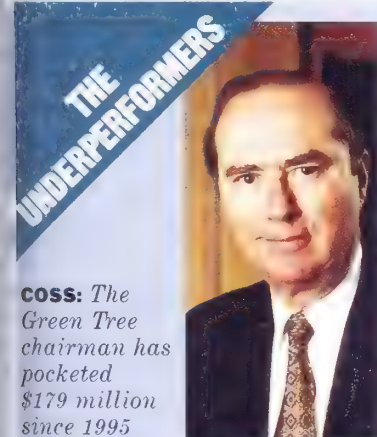
The bad news hurt Coss's wallet, too, but not enough to improve his standing in our rankings. On Mar. 25, he gave back around a third of his 1996 bonus, originally worth \$102 million in cash and shares. Since the giveback occurred in 1998, though, Green Tree did not account for it in the 1997 financial statements BUSINESS WEEK uses to calculate the rankings. Yet even if we had factored in Coss's less generous bonus, estimating it at roughly \$69 million, he would



SINEGAL: The CEO's salary held steady, while Costco's stock price tripled



GATES: His salary is a bargain—it's stock ownership that rewards him so richly



COSS: The Green Tree chairman has pocketed \$179 million since 1995



SMITHBURG: Though his pay was modest, the Snapple buy proved disastrous for Quaker Oats' ROE

have remained at the bottom of the class. Neither the company nor Coss will comment. On Apr. 7, insurer Conseco Inc. agreed to buy Green Tree.

The other underperformer is William D. Smithburg, who turned in the worst ROE relative to his compensation for the three-year period. Smithburg left Quaker Oats Co. last October after the company stumbled in the wake of his disastrous \$1.7 billion acquisition of Snapple Beverage Co. in late 1994. He and the company won't comment.

Under Quaker, sales plummeted at the once trendy Snapple. Last spring, an exasperated Smithburg finally unloaded the unit to Triarc Cos., maker of RC Cola, for a measly \$300 million. The debacle forced Quaker to take a massive charge to earnings, which led to a \$931 million loss for 1997. Although Smithburg's \$5 million total pay for 1995 to 1997 was relatively modest, the 106% negative ROE Quaker suffered for the period was simply too much to overcome.

By Larry Light in New York, with bureau reports

tutional Investors, a group representing more than 100 pension funds with assets of more than \$1 trillion, called for companies to "index" option grants, or make their value contingent on outperforming the market or a peer group. Although the proclamation has no teeth, it is significant that the members unanimously approved it.

Special Report

of a well-intended push to get—and keep—good management. Where succession was once the CEO's domain, activist investors have forced boards to take a bigger role in choosing leadership. So, directors are more readily dumping laggard CEOs and working to keep good ones.

The shift has led to one unintended side effect: When it comes time to choose a new CEO or renegotiate an old one's contract, boards are going after the same small pool of experienced CEO candidates. It's the human equivalent of the old adage "no one ever got fired for buying IBM." Few boards get criticized for choosing an experienced, well-known CEO rather than taking a shot on a promising but unproven No. 2.

"Boards are becoming more risk-averse," says pay consultant Pearl Meyer. "They are looking for a proven track record and immediate acceptance."

For those executives lucky enough to enter this charmed circle, the shift has translated into almost limitless leverage come contract time. It's the law of supply and demand—and it's a seller's market if ever there was one. As a result, more and more CEOs are demanding contracts that lock in enormous payouts. From huge signing or retention bonuses to perks such as tax planning and jet use in perpetuity, to exit packages that guarantee big bucks even if an exec is chased out of office, financial risk is virtually eliminated. Such contracts "are getting really egregious," says Carol Bowie, research director at Executive Compensation Advisory Services.

Stephen F. Wiggins, until February the chairman of Oxford Health Plans Inc.—is only the most recent example. Despite presiding over computer foul-ups that have decimated earnings and sent the once-stellar stock tumbling 73% last year, Wiggins got severance worth \$9 million when he left. His juicy deal included the continuation of his Harvard Club membership and a nearly \$2 million annual consulting salary. While such packages are becoming routine, the reaction sure wasn't: In April, the New York State Superintendent of Insurance strong-armed Oxford into withholding the pay until it proves that policyholders won't be hurt.

The story is essentially the same all over Corporate America. Sure, there were instances where laggard CEOs saw their bonuses cut or even eliminated. That happened to Eastman Kodak's George Fisher, who failed to meet earnings targets

and saw the stock slump dramatically, and to Union Pacific's Richard K. Davidson, who oversaw a disastrous year in which UP bungled its merger with Southern Pacific. But even the packages of earlier years, the cuts can amount to window dressing. When Fisher's contract was extended earlier in 1997, he got 50,000 shares of Kodak stock and 1 million new options. Although the options are under water, his stock grant is still worth over \$3 million.

BYE-BYE, BONUS. Elsewhere, too, some CEOs seem to be tightening their belts. But appearances can be deceiving. Take Lester M. Alberthal Jr., CEO of Electronic Data Systems Corp. After a year in which EDS' earnings goals weren't met and the stock underperformed, Alberthal's bonus disappeared and he got no new options. So the board gave him \$13 million in restricted shares—making up for the bonus and more.

To their credit, not all boards are relying exclusively on options to align executives' interests with those of shareholders. Many also require CEOs to own stock. According to a KPMG Peat Marwick survey, 53% of large-cap companies have adopted formal CEO guidelines, with the median target holding equal to four times salary. At Caterpillar Inc., officers

are supposed to hold shares equal to the average number of options granted in the last three option grants. If they don't, their next option grant will be reduced.

Certainly, few would dispute the value of tying a CEO's net worth to a company's stock by making him hold shares: Unlike options grants, where the worst that can happen is that there's no gain if the stock plummets, a shareholder CEO actually has real money at risk. Ownership is certainly rising. As of the end of 1997, the average large-company CEO held a \$58 million stake in his or her company, estimates Pearl Meyer & Partners Inc. up nearly 50% from 1995.

Rather than making CEOs put the money on themselves to buy stock, however, many companies

are giving it away via continuous options and stock grants or through forgivable "loans" and other helpful measures. But that defeats the whole purpose of the transaction.

Moreover, it raises some particularly thorny issues of its own: Not only can such transactions increase shareholder dilution, they also boost the level of equity ownership going to nonfounding CEOs. According to Pearl Meyer, in 1996, 17% of option grants went to proxy-level execs, and the value is rising too: In a survey of 55 large companies, nearly half made option grants worth more than \$10 million in 1997. Says corporate-governance consultant B. Kenneth West of Teachers Insurance & Annuity Assn.-College Retirement Equities Fund (TIAA-CREF): "I don't think shareholders and compensation committees recognize the degree to which some of these programs result in a transference of wealth and voting power to management."

Still, amid the pay sweepstakes, some slightly hopeful

Fortunes in the Future

These chief executives still have huge rewards to reap from stock options that have yet to be exercised. The top 20 treasure chests:

EXECUTIVE/ COMPANY	VALUE OF NONEXERCISED STOCK OPTIONS* THOUSANDS OF DOLLARS	EXECUTIVE/ COMPANY	VALUE OF NONEXERCISED STOCK OPTIONS* THOUSANDS OF DOLLARS
HENRY SILVERMAN CENDANT	\$832,972	M. DOUGLAS IVESTER COCA-COLA	\$142,916
MICHAEL EISNER WALT DISNEY	590,580 ^{††}	ELI BROAD SUNAMERICA	141,334
ECKHARD PFEIFFER COMPAQ COMPUTER	242,468	CHARLES HEIMBOLD BRISTOL-MYERS SQUIBB	139,438
RICHARD SCRUSHY HEALTHSOUTH	216,171	SUMMERFIELD JOHNSTON COCA-COLA ENTERPRISES	131,978
LAWRENCE ELLISON ORACLE	200,950	EUGENE ISENBURG NABORS INDUSTRIES	125,019
CHARLES WANG COMPUTER ASSOCIATES	187,302	STEVEN BURD SAFEWAY	120,508
JOHN WELCH GENERAL ELECTRIC	182,244	STEPHEN CASE AMERICA ONLINE	119,850
MILLARD DEXLER GAP	177,547	JOSEPH NACCHIO QWEST COMMUNICATIONS	112,500
REUBEN MARK COLGATE-PALMOLIVE	149,235	RANDALL TOBIAS ELI LILLY	108,356
LOUIS GENSTEN IBM	143,737	JOHN CHAMBERS CISCO SYSTEMS	100,495

* Based on stock price at end of company's fiscal year. † Became CEO 12/97.
†† Does not include Eisner's exercise of 7.3 million options in December, 1997 (Fiscal 1998)

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signs are on the horizon. Some companies have begun to put more stringent price hurdles into effect for their options grants. These "premium-priced options" are granted at prices above the stock price on the grant date. So the stock must appreciate before the executive starts to profit.

Special Report

At Monsanto Co., for example, the top 12 execs now have to buy their premium-priced option grants—albeit at a 50% discount to estimated value—in addition to owning five times their salary in stock by 2000. Says CEO Robert B. Shapiro: "I didn't want people to psychologically shift to protect what they have rather than looking ahead." Is a 50% stock rise all that tough in this market? "You want some stretch," says Shapiro, "but it shouldn't be so daunting that you don't participate."

"WALLPAPER." Such plans remain rare. According to KPMG Peat Marwick, just 2% of companies have implemented them. And with the Dow flirting with 9000, the question is how—and whether—the ever-upward pay spiral will moderate when the bull market finally ends. Some think shareholders and execs will feel the pain together. "The one thing that provides comfort," says Peter T. Chingos, national practice director at KPMG Peat Marwick for compensation, "is that the lion's share is coming from options. If the stock doesn't appreciate, [executives] can end up with a lot of wallpaper."

Or will they? With even run-of-the-mill CEOs now used to multimillion-dollar pay packets, few expect CEOs to settle for their relatively tiny base salaries and bonuses when a buoyant market can no longer supercharge compensation. Kevin J. Murphy, finance professor at the University of Southern California's Marshall School of Business, thinks companies will be forced to use their cash to boost their long-term cash incentive plans. "[Execs] won't just drop their stock-option plans and say

'game over,'" he says. "They'll find new games to play."

Many think that CEOs will insist on repricing their options, the equivalent of heading for the lifeboats while everyone else goes down with the ship. Repricing is considered anathema even among pay consultants; Brent M. Longnecker of Deloitte & Touche's human-resources strategy group says it's "like fingernails on a chalkboard." Yet last year's protests show that even in a good year it happens. Such companies: Guess?, U.S. Surgical, Netscape, the Learning Co., and Oxford Health Plans repriced, though not all included the CEO.

At U.S. Surgical, the practice has a particularly cynical tinge. Its repricing came last April, just two months after a February, 1997, option grant. Although CEO Leonard Hirsch—in better days, a regular on the Forbes list—didn't reprice, his wife, Executive Vice President Turi Josefsen, had 200,000 options repriced after the stock dropped to \$33.81. Originally priced at \$42.31, they were resealed at \$36.98—a 10% premium to the lower price. But that wasn't a hurdle set to challenge her. As part of the 1995 settlement of two shareholder suits alleging excessive pay, the company's three top executives agreed to set future grants at 10% above the existing market price for the next three years. So Josefsen repriced, so, using the new, lower price as her base. It's a luxury shareholders never get.

If repricing can't even be stopped at a company that has already been the target of shareholder fury, what will happen if hundreds of companies see their share price drop? "From everything I'm hearing," says W.O. Bell, chief of management policy for the Florida State Board of Administration, "it's safe to say repricing would rise exponentially if markets go down." These days, things rising exponentially just seem normal for those in the corner office.

By Jennifer Reingold in New York, with Richard Melcher in Chicago, Gary McWilliams in Houston, and bureau reports

The average boss earns 326 times what a factory worker does

Compensation Scoreboard Glossary

If the system worked perfectly, executive pay would rise when the boss delivered the goods for shareholders. And it would fall when corporate performance declined. But it doesn't always happen that way.

In this Scoreboard, **BUSINESS WEEK**, along with Standard & Poor's Compustat, attempts to measure how closely pay matches performance. The study uses two approaches: It compares an executive's total compensation with

the company's total return to shareholders in stock appreciation and dividends over three years. A second comparison measures pay against corporate profitability for the same period. Three years of data are examined to minimize the impact of single-year windfalls.

The Scoreboard companies boast market values that are among the 500 largest companies measured by market value for which 1997 compensation data

are available. Each company is assigned to one of nine industry groups. Then, each executive's pay, the company's total return to shareholders, and the company's profit record are measured against the others in the group.

Performance ratings are given only when three years of data are available. On a scale of 5, 1 indicates the best performance; 5 is the worst. The top 15% of the sample receives a 1, 25% a 2, 30% a 3, 20% a 4, and 10% a 5.

1995-97 PAY-PERFORMANCE ANALYSIS

PAY VS. SHAREHOLDERS' RETURN

TOTAL COMPENSATION is the sum of an executive's salary, bonus, and long-term compensation for the three years.

VALUE OF \$100 INVESTED is the yearend 1997 value of a \$100 investment in the company made three years earlier, including both share-price appreciation and dividends (reinvested).

RATING shows how an executive stacks up against industry peers, measured in terms of pay relative to total return to shareholders. The rating is based on an index in which the value of the investment at the end of the three-year period is divided by an executive's total pay and then compared with other executives in the same industry group.

PAY VS. CORPORATE PROFIT

ROE is the company's average return on common equity over the three-year period.

CHANGE IN ROE is the improvement or decline in the company's profitability over the 1995-97 period, expressed in terms of a percentage.

RATING shows how an executive compares with industry peers in pay for company profitability. The rating is based on an index that provides equal weight to the company's overall ROE as well as its improvement or decline during the past three years. Both these measurements are divided by an executive's total pay and then compared with others in the same industry grouping.

Footnotes: †Indicates executive retired in 1997-98 ‡May exclude option gains in earlier years e=estimated NA=not available NM=not meaningful

EXECUTIVE COMPENSATION SCOREBOARD

COMPANY	1997 SALES: \$ MILLIONS ROE: %	EXECUTIVE	1997 COMPENSATION			1995-97 PAY-PERFORMANCE ANALYSIS					
			TOTAL ANNUAL COMP. SALARY & BONUS \$000	% CHANGE FROM 1996	LONG- TERM COMP \$000	PAY VS. SHAREHOLDER RETURN			PAY VS. CORPORATE PROFIT		
						TOTAL COMP \$000	\$ VALUE OF \$100 INVESTED	RATING	ROE %	CHANGE IN ROE %	RATING
AEROSPACE & DEFENSE (INDUSTRIAL: HIGH TECH)											
BOEING	45800.0 -1.4	P.M. Condit, chmn. & CEO H.C. Stonecipher, pres. & COO	1331 3719*	0 NA	2347 12318*	9334 NA	217 NA	2 NA	4.2	-115.6	5 NA
*Includes \$15 mil. paid in total compensation by McDonnell Douglas prior to merger 8/97.											
GENERAL DYNAMICS	4062.0 16.5	N.D. Chabreja, chmn. & CEO* J.R. Mellor, chmn.†	1962 1241	41 -53	1224 9613**	7140 18636	215 NA	2 4	16.0	-2.6	2 4
*Became CEO 6/1/97. **Includes \$580,000 paid in consulting agreement upon retirement & \$840,000 paid in lieu of grant.											
LOCKHEED MARTIN	28069.0 -11.2	V.D. Coffman, vice-chmn. & CEO* N.R. Augustine, chmn. & CEO†	2163 1979**	26 -29	337 0	11456 35644	235 NA	3 5	7.4	157.2	5 5
*Became CEO 8/1/97. **Includes compensation paid until retirement on 8/1/97											
UNITED TECHNOLOGIES	24713.0 25.5	G. David, chmn. & CEO K.J. Krapek, pres.	2892 1754	17 33	9053 74	20934 6178	246 NA	3 3	21.3	70.2	3 2
AIRLINES (TRANSPORTATION)											
AMERICAN AIRLINES	18570.0 16.4	R.L. Crandall, chmn., pres. & CEO D.J. Carty, exec. v-p	806* 648*	-51 -47	0* 1471*	8688 6924	241 NA	3 4	13.7	215.7	2 2
May contain data from a preliminary source. *1997 bonus and long-term award have not yet been determined.											
DELTA AIR LINES	13946.0 27.1	R.W. Allen, chmn., pres. & CEO† R.W. Coggin, exec. v-p	577 554	-43 3	4758 1350	9036 3855	237 NA	3 2	13.8	NM	1 1
NORTHWEST AIRLINES	10225.8 NM	J.H. Dasburg, pres. & CEO M.E. Levine, exec. v-p	1018 713	12 19	5835 1462	23132 8964	304 NA	3 4	NM	NM	NA NA
UNITED STATES AIRLINES	17378.0 37.7	G. Greenwald, chmn. & CEO J.A. Edwardson, pres. & COO	1490 976	0 4	0 0	6257 4083	423 NA	1 1	NM	NM	NA NA
APPLIANCES & HOME FURNISHINGS (CONSUMER PRODUCTS)											
3M	2909.2 18.6	H.M. Cornell Jr., chmn. & CEO B.L. Gaddy, sr. v-p†	604* 407**	4 33	1937 0	4950 NA	251 NA	1 NA	17.7	0.7	2 NA
*Excludes \$684,786 bonus paid in 19,946 stock options. **Excludes \$60,288 salary & \$125,206 bonus paid in stock options.											
AMERILPOOL	8617.0 -2.6	D.R. Whitwam, chmn. & CEO W.D. Marohn, pres. & COO	2060 1138	47 50	1398 682	6968 3573	118 NA	3 3	5.5	-128.3	5 5
AUTOMOTIVE (CONSUMER PRODUCTS)											
ACURA	8769.4 21.7	S.J. Morcott, chmn. & CEO J.M. Magliochetti, pres. & COO	2319 1150	16 18	3098 651	10859 4284	221 NA	3 2	22.6	-10.6	3 2
BUICK	6751.9 23.0	M.C. Pigott, chmn. & CEO D.J. Hovind, pres.	743* 599*	-7 -36	324 460	2639 3413	282 NA	1 1	19.3	32.1	1 1
*1997 bonus has not been determined.											
BANKS & BANK HOLDING COMPANIES (FINANCIAL SERVICES)											
SOUTH WESTBANK CORPORATION	1643.8 16.3	C.D. Ritter, chmn., pres. & CEO E.W. Stephenson Jr., sr. exec. v-p	1616 591	16 11	293 265	8131 3093	353 NA	2 2	14.0	68.1	2 1
WELLS FARGO BANK	13219.1 12.6	J.B. McCoy, chmn. & CEO R.J. Lehmann, pres.	2840 1692	10 17	5278* 3620**	14248 8973	262 NA	3 4	15.1	-6.4	3 3
*Includes \$4 mil. in special recognition award. **Includes \$3 mil. in special recognition award.											
CITIBANK OF NEW YORK	5697.0 21.9	J.C. Bacot, chmn.† T.A. Renyi, pres. & CEO*	8302 5521	55 74	23193 915	44479 12014	437 NA	4 3	19.9	24.3	4 3
*Became CEO 7/1/97											
CITIBANK AMERICA	23585.0 16.2	D.A. Coulter, chmn. & CEO M.J. Murray, pres.	5238 2575	48 65	1444 4698	12004 10313	400 NA	3 3	14.9	32.8	3 3
CITIBANK BOSTON	6727.2 19.6	C.K. Gifford, chmn. & CEO W.M. Crozier Jr., chmn.†	3300 2675	10 64	6316 11668	21957 NA	397 NA	3 NA	16.3	27.2	3 NA
CITIBANK NEW YORK	12176.0 16.2	F.N. Newman, chmn., pres. & CEO R.K. Doherty, vice-chmn.	10937 9202	23 29	1076 3016	23594 NA	238 NA	4 NA	10.9	18.8	4 NA
CITIBANK MANHATTAN	30381.0 17.6	W.V. Shipley, chmn. & CEO T.G. Labrecque, pres. & COO	6148 5660	9 9	5137 5936	26136 26989	332 NA	4 5	15.0	41.2	4 4
CITICORP	34697.0 17.9	J.S. Reed, chmn. & CEO M.A. Taylor, exec. v-p	4000 1442	15 NA	90 6322	55838 NA	325 NA	5 NA	18.8	-20.8	5 NA

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EXECUTIVE COMPENSATION SCOREBOARD

COMPANY		EXECUTIVE	1997 COMPENSATION			1995-97 PAY-PERFORMANCE ANALYSIS					
			TOTAL ANNUAL COMP		LONG-TERM COMP \$000	PAY VS. SHAREHOLDER RETURN			PAY VS. CORPORATE PROFIT		
			SALARY & BONUS \$000	% CHANGE FROM 1996		TOTAL COMP \$000	\$ VALUE OF \$100 INVESTED	RATING	ROE %	CHANGE IN ROE %	RATING
COMERICA	3175.4 20.4	E.A. Miller, chmn. & CEO M.T. Monahan, pres. May contain data from a preliminary source.	1834 1234	4 0	1784 206	9113 3637	408	2 2	17.8	26.2	2 1
CORESTATES FINANCIAL	4277.6 25.1	T.A. Larsen, chmn. & CEO R.B. Greco, pres.	1542 826	41 23	0 6014	16182 11521	346	3 3	20.6	137.3	2 2
CRESTAR FINANCIAL	1997.0 15.0	R.G. Tilghman, chmn. & CEO J.M. Wells III, pres. & COO	2162 1271	55 51	800 0	7799 3527	334	2 2	13.2	0.2	2 2
FIFTH THIRD BANCORP	1923.8 17.6	G.A. Schaefer Jr., pres. & CEO S.J. Schrantz, exec. v-p	1679 722	21 11	1560 780	6924 3121	406	1 1	16.6	0.8	2 1
FIRST CHICAGO NBD	10098.0 19.4	V.G. Istock, chmn., pres. & CEO T.H. Jeffs II, vice-chmn.	2028 1238	-2 5	3417 2304	11569 8414	339	3 3	16.6	16.4	3 3
FIRST SECURITY	1503.4 15.6	S.F. Eccles, chmn. & CEO M.J. Evans, pres. & COO	769 569	9 11	2548 804	4728 2739	455	1 1	14.3	-0.8	2 2
FIRST TENNESSEE NATIONAL	1609.4 20.7	R. Horn, pres. & CEO J.K. Glass, pres. sub. *Excludes \$30,000 salary paid in form of options.	848 537*	16 20	15 10	2427 2035	360	1 1	19.5	5.9	1 1
FIRST UNION	14329.0 15.2	E.E. Crutchfield, chmn. & CEO J.R. Georgius, vice-chmn.	3179 2199	2 2	16072 3779	31694 12952	274	4 4	15.3	-9.1	4 4
FIRSTAR	1892.6 17.5	R.L. Fitzsimonds, chmn. J.A. Becker, pres.	1015 722	26 24	1824 1320	5635 4010	349	1 2	15.8	9.8	2 2
FLEET FINANCIAL GROUP	8095.0 16.9	T. Murray, chmn. & CEO R.J. Higgins, pres. & COO	3822 1883	18 41	5693 1913	18015 8908	259	4 4	13.5	-15.2	4 4
HUNTINGTON BANCSHARES	2324.3 14.5	F.G. Wobst, chmn. & CEO Z. Sofia, pres. & COO	1680 914	12 10	143 763	6132 5988	292	2 3	16.0	-15.9	2 3
KEYCORP	6568.0 17.7	R.W. Gillespie, chmn. & CEO H.L. Meyer III, pres. & COO	2085 1265	54 85	1721 1702	8561 5079	316	3 2	16.4	-3.9	2 2
MARSHALL & ILSLEY	1742.5 12.5	J.B. Wigdale, chmn. & CEO D.J. Kuester, pres.	1152 971	21 25	780 1996	4262 4989	351	1 2	14.5	43.3	1 2
MBNA	4523.9 32.3	A. Lerner, chmn. & CEO C.M. Cawley, pres.	4500 4623	0 1	1564 22461	16577 43709	417	3 5	29.0	11.4	2 4
MELLON BANK	5134.0 20.5	F.V. Cahouet, chmn., pres. & CEO C.M. Condron, pres. & COO *Excludes 25% of bonus paid in restricted stock.	2478* 993*	22 13	15020 2609	30289 6935	446	4 2	19.5	111.5	3 2
MERCANTILE BANCORPORATION	2256.9 8.7	T.H. Jacobsen, chmn., pres. & CEO W.R. Adams, sr. exec. v-p	1670 661	32 48	0 1519	7419 4097	323	2 2	11.8	-42.4	3 3
MORGAN (J.P.)	17701.0 13.4	D.A. Warner III, chmn. R.G. Mendoza, vice-chmn.	3042 2565	-6 -14	5926 1733	24702 18189	225	4 4	13.5	1.4	4 4
NATIONAL CITY	5152.1 18.9	D.A. Daberkho, chmn. & CEO V.A. DiGirolamo, vice-chmn. *Excludes portion of bonus paid in restricted stock valued at \$436,514.	1070* 798	11 18	4416 3380	11129 6373	286	3 3	17.3	9.9	3 2
NATIONSBANK	21581.0 14.4	H.L. McColl Jr., CEO A.B. Craig III, chmn.* *Joined company 1/7/97.	4500 4491	11 NA	0 12887	12056 NA	294	3 NA	15.7	-5.8	3 NA
NORTHERN TRUST	2267.3 18.8	W.A. Osborn, chmn. & CEO B.G. Hastings, pres. & COO	1623 1119	62 44	1644 1520	6497 5321	423	1 2	17.7	19.4	2 2
NORWEST	9659.7 19.5	R.M. Kovacevich, chmn. & CEO L.S. Biller, pres. & COO	3286 2533	5 64	8141 4006	23219 11288	359	4 3	19.0	-15.8	4 3
PNC BANK	6859.2 19.2	T.H. O'Brien, chmn. & CEO J.E. Rohr, pres.	2953 1556	40 15	6174 1768	15156 7097	309	3 3	14.4	38.9	3 3
PROVIDIAN FINANCIAL	1217.1 32.0	S.J. Mehta, chmn., pres. & CEO S.A. Barad, exec. v-p†	2066 555	37 25	26298 928	31646 2375	NA	NA NA	NA	NA	NA NA
REPUBLIC NEW YORK	3738.2 14.4	W.H. Weiner, chmn. & CEO E. Saal, vice-chmn.	1726 1920	11 37	400 480	5286 5149	269	2 3	13.0	-7.3	2 3
SOUTHTRUST	2502.8 14.0	W.D. Malone Jr., chmn. & CEO J.W. Banton, pres.	1706 542	3 8	984 1034	7077 3267	385	2 1	14.2	-8.3	2 2
STAR BANC	1009.1 21.5	J.A. Grundhofer, chmn., pres. & CEO D.M. Moffett, exec. v-p & CFO	1688 606	7 4	2862 2107	9443 3798	510	2 1	18.9	32.3	2 1
STATE STREET	3428.0 19.0	M.N. Carter, chmn. & CEO N.A. Lopardo, vice-chmn.	2310 2077	54 25	3539 773	13960 6820	423	3 3	17.0	13.1	3 3
SUMMIT BANCORP.	2366.6 14.2	T.J. Semrod, chmn. & CEO R.G. Cox, pres.	1872 1199	27 30	6018 1873	11769 NA	360	3 NA	13.1	17.3	3 NA
SUNTRUST BANKS	4585.0 12.8	J.B. Williams, chmn. & CEO L.P. Humann, pres.* *Became CEO 3/21/98.	1366 738	21 11	720 600	10044 6806	318	3 3	12.9	-15.2	3 3
SYNOVUS FINANCIAL	1214.9 19.1	J.H. Blanchard, chmn. & CEO J.D. Yancey, vice-chmn.	1078 889	4 31	58 60	3920 2953	429	1 1	17.8	12.5	1 1
U.S. BANCORP	6908.8 14.1	J.F. Grundhofer, pres. & CEO G.B. Cameron, chmn. *Includes \$5.5 mil. in connection with the merger. Joined company 8/1/97.	2692 2116	30 NA	17921 18897*	42969 NA	365	4 NA	19.8	16.5	4 NA

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EXECUTIVE COMPENSATION SCOREBOARD

COMPANY	1997 SALES: \$ MILLIONS ROE %	EXECUTIVE	1997 COMPENSATION			1995-97 PAY-PERFORMANCE ANALYSIS					
			TOTAL ANNUAL COMP SALARY & BONUS \$000	% CHANGE FROM 1996	LONG- TERM COMP. \$000	PAY VS. SHAREHOLDER RETURN TOTAL COMP \$000	\$ VALUE OF \$100 INVESTED	RATING	PAY VS. CORPORATE PROFIT ROE %	CHANGE IN ROE %	RATING
UNION PLANTERS	1778.3	B.W. Rawlins Jr., chmn. & CEO	1534	48	0	7546	360	[2]	12.4	63.4	[2]
	12.7	J.W. Moore, pres. & COO	1096	65	0	4820		[2]			[2]
WACHOVIA	5269.6	L.M. Baker Jr., pres. & CEO	1184	12	1066	6457	276	[2]	15.6	-17.2	[2]
	13.5	W.E. Leonard Jr., sr. exec. v-p	734	8	1060	4571		[3]			[2]
WELLS FARGO	9608.0	P. Hazen, chmn., pres. & CEO	2858	0	20173	29698	250	[5]	14.7	-61.6	[5]
	9.0	R.L. Jacobs, vice-chmn.	1440	21	6466	12605		[4]			[5]
6 BEVERAGES (CONSUMER PRODUCTS)											
ANHEUSER-BUSCH	11066.2	A.A. Busch III, chmn., pres. & CEO	1799	-26	7191	19369	190	[4]	26.0	24.8	[3]
	29.2	P.T. Stokes, v-p	950	-21	2576	8732		[4]			[3]
COCA-COLA	18868.0	R.C. Goizueta, chmn. & CEO*	4052	-22	107781	140812	268	[5]	56.2	15.8	[4]
	56.5	M.D. Ivester, chmn. & CEO**	2856	48	9920	36970		[5]			[3]
*Passed away 10/18/97. **Became CEO 10/18/97.											
COCA-COLA ENTERPRISES	11278.0	S.K. Johnston Jr., chmn. & CEO	2095	-57	475	13926	597	[2]	7.6	85.4	[3]
	9.5	H.A. Schimberg, pres. & COO	1831	-61	421	25975		[4]			[4]
PEPSICO	20917.0	R.A. Enrico, chmn. & CEO	2807	-9	0	20586	227	[4]	20.9	-9.7	[3]
	23.5	C.E. Weatherup, chmn. & CEO-Pepsi-Cola	2018	18	8196	NA		NA			NA
7 BUILDING (INDUSTRIAL: LOW TECH)											
PPG INDUSTRIES	7379.0	J.E. Dempsey, chmn. & CEO†	1365	-34	1176	8130	166	[3]	29.4	41.4	[1]
	28.5	R.W. LeBoeuf, chmn. & CEO*	1257	11	2883	8361		[4]			[3]
*Became CEO 7/1/97											
SHERWIN-WILLIAMS	4881.1	J.G. Breen, chmn. & CEO	1646	7	2084	9257	174	[3]	16.4	-7.6	[3]
	16.4	T.A. Commes, pres. & COO	1068	5	609	5707		[3]			[3]
8 CHEMICALS (INDUSTRIAL: LOW TECH)											
AIR PRODUCTS & CHEMICALS	4751.7	H.A. Wagner, chmn., pres. & CEO	1651	36	1589	7076	194	[2]	16.8	78.4	[2]
	18.9	J.J. Kaminski, exec. v-p	727	29	664	3841		[2]			[2]
DOW CHEMICAL	20918.0	W.S. Stavropoulos, pres. & CEO	1835	22	3128	10797	169	[3]	24.0	106.5	[2]
	23.4	A.J. Carbone, exec. v-p	1107	16	1158	4971		[3]			[2]
DUPONT	45079.0	J.A. Kroi, CEO*	3075	28	11141	19063	232	[4]	32.1	0.5	[3]
	21.7	A.W. Dunham, exec. v-p	2118	31	431	9418		[4]			[3]
*Left office 2/1/98											
HERCULES	1866.0	R.K. Elliott, chmn. & CEO	1730	99	6204	12504	137	[4]	36.1	93.4	[1]
	41.0	V.J. Corbo, pres. & COO	1026	111	1306	9019		[4]			[2]
IMC GLOBAL	2988.6	R.E. Fowler Jr., pres. & CEO*	973	42	480	NA	154	NA	11.2	NM	NA
	4.5	W.F. Bueche, chmn.	618	-37	299	4972		[3]			[3]
*Became CEO 7/2/97											
INTL. FLAVORS & FRAGRANCES	1426.8	E.P. Grisanti, chmn. & pres.	1395	25	0	3783	121	[2]	20.3	-5.8	[1]
	21.1	B.D. Chadbourne, sr. v-p†	686	118	0	NA		NA			NA
MONSANTO	7514.0	R.B. Shapiro, chmn. & CEO	1834	-37	47491	56434	347	[5]	12.5	-66.0	[5]
	7.2	R.U. De Schutter, vice-chmn.†	1225	-6	8537	13374		[3]			[4]
MORTON INTERNATIONAL	2560.0	S.J. Stewart, chmn. & CEO	4380	194	5291	14805	173	[4]	17.4	-9.8	[4]
	14.6	W.E. Johnston, pres. & COO	1791	111	1718	6442		[3]			[3]
PRAXAIR	4735.0	H.W. Lichtenberger, chmn. & CEO	1516	-23	4468	23466	226	[4]	19.2	-19.0	[4]
	19.6	E.G. Hotard, pres. & COO	815	-28	453	11031		[4]			[4]
ROHM & HAAS	3999.0	J.L. Wilson, chmn. & CEO	1939	54	1334	6714	180	[2]	21.3	40.6	[2]
	24.3	J.P. Mulrone, pres.	1184	37	1463	5028		[3]			[2]
UNION CARBIDE	6502.0	W.H. Joyce, chmn., pres. & CEO	1809	-4	1086	6587	155	[2]	33.5	14.0	[1]
	28.3	J.E. Geoghan, v-p	690	0	0	4336		[3]			[1]
9 CONGLOMERATES (INDUSTRIAL: LOW TECH)											
ALLEGHENY TELEDYNE	3745.1	R.P. Simmons, chmn., pres. & CEO*	1631	NA	213	NA	274	NA	32.0	NM	NA
	29.8	A.H. Aronson, exec. v-p†	803	20	415	3608		[2]			[1]
*Became CEO 2/12/97											
ALLIEDSIGNAL	14472.0	L.A. Bossidy, chmn. & CEO	5155	7	23082	48512	239	[5]	25.1	4.8	[4]
	26.7	F.M. Poses, vice-chmn.	1259	7	3973	15743		[5]			[4]
GENERAL ELECTRIC	88540.0	J.F. Welch, chmn. & CEO	8069	28	31825	89577	307	[5]	23.1	6.3	[4]
	23.8	P. Fresco, vice-chmn.	3700	21	19064	47890		[5]			[4]
HARCOURT GENERAL	3823.6	Richard A. Smith, chmn. & CEO*	1538	21	0	4088	163	[1]	6.5	-291.2	[5]
	-17.8	Robert A. Smith, pres. & co-CEO†	935	127	0	1692		[1]			[5]
*Became CEO 1/15/97.											
IKON OFFICE SOLUTIONS	5362.3	J.E. Stuart, chmn. & CEO	900	-50	576	8273	114	[3]	9.9	51.6	[3]
	7.7	J.J. Forese, exec. v-p	425	-56	0	NA		NA			NA
ITT INDUSTRIES	8777.1	D.T. Engen, chmn., pres. & CEO	1793	4	1854	8527	187	[2]	14.1	347.0	[3]
	13.8	L.J. Giuliano, sr. v-p	707	7	851	4425		[2]			[2]
TENNECO	7220.0	D.G. Mead, chmn. & CEO	1346*	-50	950	9569	119	[4]	12.6	-34.2	[4]
	14.3	P.T. Stecko, COO	1172	29	797	4781		[4]			[4]
*Received options in lieu of a bonus.											

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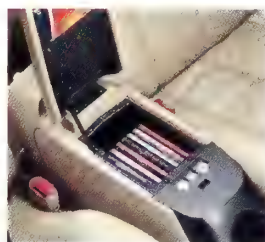
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EXECUTIVE COMPENSATION SCOREBOARD

COMPANY		EXECUTIVE	1997 COMPENSATION			1995-97 PAY-PERFORMANCE ANALYSIS					
			TOTAL ANNUAL COMP		LONG-TERM COMP \$000	PAY VS. SHAREHOLDER RETURN			PAY VS. CORPORATE PROFIT		
			SALARY & BONUS \$000	% CHANGE FROM 1996		TOTAL COMP \$000	\$ VALUE OF \$100 INVESTED	RATING	ROE %	CHANGE IN ROE %	RATING
TEXTRON	10544.0	J.F. Hardymon, chmn. & CEO	2712	2	3730	15043	264	3	15.5	14.9	3
	17.3	L.B. Campbell, pres. & COO	1400	17	1965	10739		4			4
TRW	10831.0	J.T. Gorman, chmn. & CEO	5503	9	1398	17625	174	4	8.6	-116.9	5
	-3.1	P.S. Hellman, pres. & COO	3045	8	213	8680		4			5

10 CONTAINERS (INDUSTRIAL: LOW TECH)

AVERY DENNISON	3345.7 24.5	C.D. Miller, chmn. & CEO P.M. Neal, pres. & COO	2105 1283	12 10	9116 2824	19725 8533	269	3 3	21.1	63.0	3 3
CROWN CORK & SEAL	8494.6 9.2	W.J. Avery, chmn. & CEO M.J. McKenna, pres. & COO	1283 657	28 67	0 0	4152 2641	138	1 2	7.7	-4.5	3 3
OWENS-ILLINOIS	4658.5 21.4	J.H. Lemieux, chmn. & CEO L.A. Wesselmann, sr. v-p & CFO	1229 539	-13 6	13777 2192	18577 3960	345	3 1	27.0	-2.1	3 2

11 DRUGS (CONSUMER PRODUCTS)

ABBOTT LABORATORIES	11883.5 41.9	D.L. Burnham, chmn. & CEO T.R. Hodgson, pres. & COO	2647 1688	9 12	6836 3157	15445 8708	213	3 4	39.8	11.9	2 2
AMERICAN HOME PRODUCTS	14196.0 27.4	J.R. Stafford, chmn., pres. & CEO R.G. Blount, sr. exec. v-p	2700 1420	10 9	18244 6756	44291 20357	267	4 5	28.2	-23.8	4 4
AMGEN	2401.0 30.1	G.M. Binder, chmn. & CEO K.W. Sharer, pres. & COO	1437 833	-12 -31	8864 2543	44101 10444	183	5 4	32.6	20.1	4 3
BAXTER INTERNATIONAL	6138.0 11.5	V.R. Loucks Jr., chmn. & CEO H.M. Jansen Kraemer Jr., pres.	2174 1127	16 66	6196 1184	13894 3866	210	3 2	14.8	-28.5	4 4
BECTON, DICKINSON	2856.4 22.3	C. Castellini, chmn., pres. & CEO J.W. Galiardo, vice-chmn.	1597 777	18 6	353 413	5143 3265	216	2 2	20.6	46.2	2 1
BRISTOL-MYERS SQUIBB	16701.0 46.3	C.A. Heimbald Jr., chmn. & CEO K.E. Weg, exec. v-p	2803 1194	21 14	26409 8578	38151 11918	358	4 3	40.3	43.3	3 2
GENENTECH	947.6 6.4	A.D. Levinson, pres. & CEO W.D. Young, COO	1040 635	30 9	0 0	2515 3379	133	1 3	7.4	-31.1	3 4
GUIDANT	1328.2 25.8	R.W. Dollens, pres. & CEO J.M. Cornelius, chmn.	760 1437	30 21	0 0	3052 5224	782	1 1	22.3	-26.0	2 3
JOHNSON & JOHNSON	22629.0 26.7	R.S. Larsen, chmn. & CEO R.N. Wilson, vice-chmn.	3574* 2662**	27 14	8431 7737	20145 18446	252	3 5	26.6	-5.1	3 4
*Includes \$980,552 dividend equivalent. **Includes \$909,371 dividend equivalent.											
LILLY (ELI)	8517.6 -8.3	R.L. Tobias, chmn. & CEO S. Taurel, pres. & COO	2679 1634	12 10	1661 2824	14658 9918	455	2 2	13.5	-137.7	5 5
MEDTRONIC	2560.2 23.4	W.W. George, chmn. & CEO A.D. Collins Jr., pres. & COO	1107 686*	9 -13	1431 934	6577 4205	383	1 1	26.1	6.3	2 2
*Excludes \$100,000 bonus paid as 5,777 stock options.											
MERCK	23636.9 36.6	R.V. Gilmartin, chmn., pres. & CEO E.M. Scolnick, exec. v-p	2600 1514	13 3	0 3403	7000 13802	296	2 4	32.5	36.0	2 3
Pfizer	12504.0 29.9	W.C. Steere Jr., chmn. & CEO H.A. McKinnell Jr., exec. v-p	3880 1796	10 17	24240 7791	49915 15947	406	4 4	28.6	-0.5	4 4
PHARMACIA & UPJOHN	6710.0 5.0	F. Hassan, pres. & CEO* G.A. Ando, exec. v-p	1323 816	NA -9	10080 0	NA 2444	190	NA 1	8.4	-75.2	NA 5
*Joined company and became CEO 5/10/97.											
SCHERING-PLOUGH	6778.0 51.2	R.J. Kogan, pres. & CEO R.P. Luciano, chmn.	2242 2537	13 5	11797 8463	28569 30305	358	4 5	58.3	-12.6	3 3
STRYKER	980.1 20.5	J.W. Brown, chmn., pres. & CEO R.A. Elenbaas, v-p	1050 610	11 17	0 0	2775 1999	204	1 1	19.8	1.3	1 1
WARNER-LAMBERT	8179.8 30.7	M.R. Goodes, chmn. & CEO L.J. de Vink, pres. & COO	2682 1640	14 20	8386* 3185	19769 9761	346	3 3	31.4	-19.7	3 3
*Includes \$7.2 mil. payments for cash awards.											

12 ELECTRICAL & ELECTRONICS (INDUSTRIAL: HIGH TECH)

AMP	5745.0 15.6	W.J. Hudson Jr., pres. & CEO J.E. Marley, chmn.	1380 1135	64 68	1980 1605	8275 6675	124	3 3	13.8	-1.4	2 3
ANALOG DEVICES	1282.2 16.2	J.G. Fishman, pres. & CEO R. Stata, chmn.	1284 857	-7 -33	6545 4632	15004 8310	236	3 3	18.1	13.3	3 3
COOPER INDUSTRIES	5288.8 15.3	H.J. Riley Jr., chmn., pres. & CEO R.E. Jackson Jr., exec. v-p	1594 780	7 6	0 0	4056 2048	158	2 1	16.1	73.3	1 1
EATON	7563.0 22.4	S.R. Hardis, chmn. & CEO A.M. Cutler, pres. & COO	2325 1577	33 30	1085 1078	8317 6570	195	2 3	19.6	13.0	2 3
HARRIS	3917.5 13.6	P.W. Farmer, chmn., pres. & CEO W.E. Cantrell, pres.-sub.	334 118	19 6	2841 594	8475 3559	230	2 2	13.0	32.2	2 2
INTEL	25070.0 36.0	A.S. Grove, chmn. & CEO C.R. Barrett, pres. & COO	3255 2555	8 11	48958 0	157985 20862	443	5 3	32.0	45.8	4 3
LINEAR TECHNOLOGY	425.9 24.6	R.H. Swanson Jr., pres. & CEO C.B. Davies, v-p & COO	1090 866	-9 -13	406* 2996*	4406 7981	236	1 3	27.5	-3.2	1 2

*1996 stock options canceled & exchanged for new options in 1997



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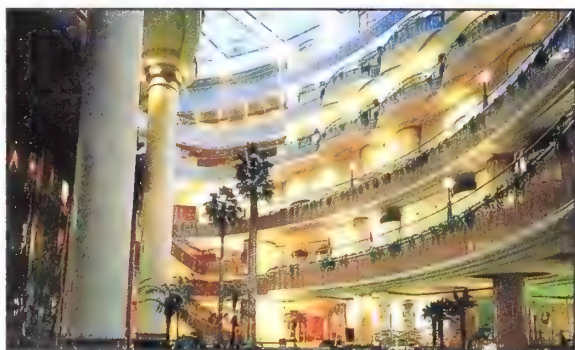
clearest sound quality* on calls back to the States. Always look for hotels that offer the convenience of the

AT&T Speed Dial feature. It's another innovation that makes your life easier from

the world's most powerful network. AT&T.



Available at these fine Asia/Pacific hotels:



Sunshine Hotel
Shenzhen, China
Tel.: 86 755 223 3888

A deluxe commercial hotel and the first 5-Star hotel in the center of Shenzhen City. Its 371 guest rooms include 64 executive rooms with private room safe and fax. Daily free shuttle bus between Hong Kong and Shenzhen Railway Station.



Holiday Inn Crowne
Plaza Beijing
HOLIDAY INN
WORLDWIDE
Beijing, China
Tel.: 86 1 651 333 88

In the heart of the city, this hotel displays a fine collection of traditional and contemporary Chinese art in its Art Salon and Gallery. Tiananmen Square and the Forbidden City are just a short distance away. The Grand Ballroom and Executive Boardroom can accommodate 350 people.



Beijing
北京国际艺苑皇冠假日饭店

*Based on 1997 customer preference study compared to other U.S. carriers. Credit card calling subject to availability. Payment terms subject to your credit card agreement. Collect calling is available to the U.S. only.



A 63-story building that is the tallest 5-Star hotel in China. It is located in the growing commercial and financial center of Guangzhou. Near the major recreational and shopping area. Features ultra-modern facilities with deluxe accommodations, international cuisine and fashionable nightlife.

Gitic Plaza Hotel
Guangzhou, China
Tel.: 86 20 8331 1888



广东国际大酒店
GITIC PLAZA HOTEL
★★★★★



The first 4-Star international hotel in Qingdao with 464 luxury rooms and suites. Conveniently located to major commercial centers, tourist attractions and historical sites. Chinese, Japanese and international restaurants and bars. Flexible function rooms.

Hotel Equatorial
Qingdao
Qingdao, China
Tel.: 86 532 581 6015
/6025

青島貴都大飯店
 **hotel Equatorial**
QINGDAO



Haitian Hotel
Qingdao, China
Tel.: 86 532 387 1888

A 5-Star hotel located 30 minutes from the airport in a prime area of the city. Renowned for its gracious Chinese hospitality, the hotel has a Business Center, meeting and conference rooms, two executive floors, six restaurants, pool, tennis courts, sauna, gym, discotheque, karaoke, online office and a shopping arcade.



HAITIAN HOTEL
QINGDAO P.R.C.



Grand Regency Hotel
Qingdao, Shandong, China
Tel.: 86 588 1818

A fine hotel that features a variety of meeting spaces. The ballroom can comfortably accommodate 800 people. The International Convention Center can hold 400 people. Three Convention Centers are suitable for meetings for 20 to 40 guests. Meeting facilities include a wide range of audio-visual and technical equipment.





Ramada Hotel Wuhan
Wuhan, China
Tel.: 86 27 578 7968

Located in the central business and commercial district. Adjacent to the 150-acre Fountain Amusement Park and 15 miles from the Wuhan Tianhe International Airport. All suites are equipped with direct fax lines and machines. All rooms have safes, data and telephone ports.



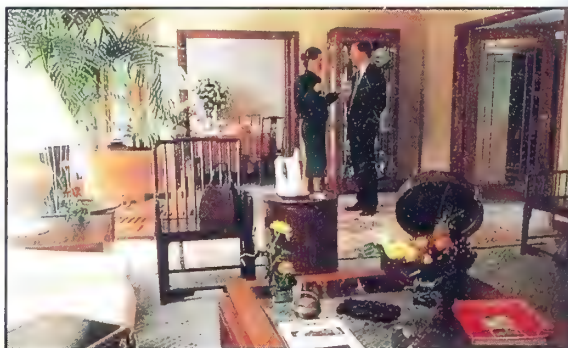
Yindo Hotel
Zhuhai, China
Tel.: 86756 888 3388

The only 5-Star business hotel in the expanding special economic zone of Zhuhai. Towering over the bustling business district, the hotel has unique architecture, with overall facilities of international standard. Just 70 minutes from Hong Kong by hydrofoil, 5-minute walk to Macau border, 10 fully equipped meeting rooms are available.



Holiday Inn Lido Beijing
Beijing, China
HOLIDAY INN WORLDWIDE
Tel.: 86 1 643 766 88

Extensive conference facilities with 1,000 person Grand Ballroom and a 24-hour Business Center with Internet service. Executive Club Floor creates a haven of comfort and relaxation in a quiet, private atmosphere, offering international service standards.



Kempinski Hotel Beijing Lufthansa Center
LEADING HOTELS OF THE WORLD
Beijing, China
Tel.: 86 1 6465 3388

The Kempinski Hotel Complex is located in the embassy and commercial district. It features eight restaurants, three bars, two fitness centers, indoor pool, outdoor tennis courts, offices, apartments, supermarket and a department store. The Jade Ballroom accommodates 1,000 people.





OMNI Batavia Hotel
Jakarta, Indonesia
Tel.: 62 21 690 4118

A premier 4-Star international business hotel, the OMNI is conveniently located in the Glodok downtown business district within the historical area known as "Old Batavia." You will find 38 impeccably appointed rooms with fine dining establishments waiting you in the magnificent colonial style structure.

HOTEL OMNI BATAVIA
 JAKARTA, INDONESIA



Holiday Inn Crowne Plaza Jakarta
Jakarta, Indonesia
HOLIDAY INN WORLDWIDE
Tel.: 62 21 526 8833

Strategically located in Jakarta's busy Golden Triangle business district and only minutes from Soekarno-Hatta International airport, this 5-Star hotel offers 100% guest satisfaction amidst a warm and friendly atmosphere. Its excellent array of restaurants and bars, combined with its superb banquet facilities and business services, makes it the first choice hotel of discerning business travelers.

Holiday Inn
CROWNE PLAZA™
JAKARTA



Park Place Hotel
Cebu City, Philippines
Tel.: 6332 253 1131

Standing majestically in front of Fuente Osmena, Park Place Hotel has a wide range of luxurious accommodations to choose from. There are studios, standard rooms, executive rooms and suites. All rooms have air-conditioning, showers and cable television. Meeting facilities include conference rooms with the latest audiovisual equipment.

**PARK
 PLACE**
HOTEL
In the heart of it all



Golden China Hotel
Taipei, Taiwan
Tel.: 886 2 2521 5151

A 220-room hotel located in the city center. Air conditioning, refrigerator, in-room safe. Conference rooms for various sized meetings. Tour information desk, car rental on site. Business Service Center, several restaurants, concierge, 24-hour room service.





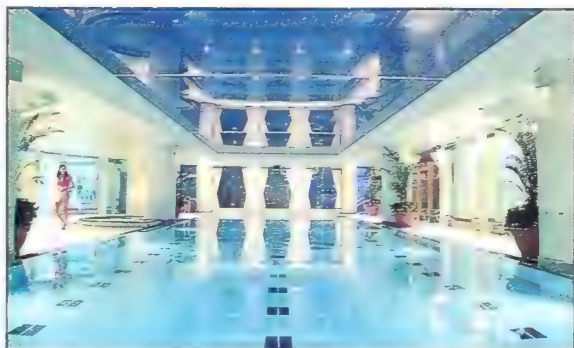
Palm Courtt Bangkok
ASCOTT INTERNATIONAL
Bangkok, Thailand
Tel.: 662 267 4050

A stylishly furnished apartment style serviced hotel. Spacious interiors, fully equipped kitchens and all modern conveniences. Located in the heart of Bangkok, it is within easy walking distance of the financial center, entertainment, shopping, hospitals, embassies and restaurants. It is the ideal place to conduct business and entertain friends and associates.



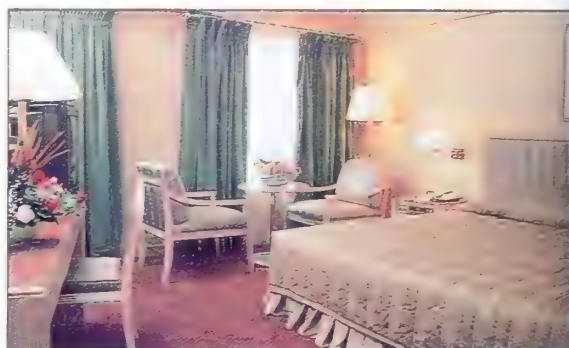
Garden Plaza Hotel
Ho Chi Minh City,
Vietnam
Tel.: 848 842 1111

Near the business district and international convention center. 157 rooms and suites with an executive floor and lounge. Business center, conference and banquet rooms, pool, gym and a variety of restaurants and bars. Rooms are sound-proofed, air conditioned, with satellite TV, minibar, bath, personal safe, radio, hairdryer and spacious desk.



Hotel Amiga
Seoul, Korea
Tel.: 82 2 3440 8000

A 200-room, 5-Star hotel with a European feel, located in the heart of Seoul's Kangnam business and entertainment district. Business accommodations include three function rooms catering up to 400 people, two business centers with fax machine, notebook computer and fax modem. Complimentary welcome beverage for AT&T Calling Card customers.



Holiday Inn Seoul
Seoul, Korea
HOLIDAY INN WORLDWIDE
Tel.: 82 2 717 9441

All 367 rooms and suites have individual temperature control, TV, radio, refrigerator with minibar, private bath with tub and shower. Meeting and banquet rooms can accommodate 1,000 and have event reader board, blackout drapes and adjustable lighting.

Outdoor function rooms available.



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EXECUTIVE COMPENSATION SCOREBOARD

COMPANY	1997 SALES \$ MILLIONS ROE %	EXECUTIVE	1997 COMPENSATION			1995-97 PAY-PERFORMANCE ANALYSIS					
			TOTAL ANNUAL COMP SALARY & BONUS \$900	% CHANGE FROM 1996	LONG- TERM COMP \$900	PAY VS. SHAREHOLDER RETURN			PAY VS. CORPORATE PROFIT		
						TOTAL COMP. \$900	\$ VALUE OF \$100 INVESTED	RATING	ROE %	CHANGE IN ROE %	RATING
XIM INTEGRATED PRODUCTS	488.0 29.1	J.F. Gifford, chmn., pres. & CEO T. Doluca, v-p† *1997 bonus has not been determined.	264* 170*	-75 -46	9808 4061	24712 5232	394	3 1	29.6	57.3	2 1
CRON TECHNOLOGY	3742.0 11.1	S.R. Appleton, chmn., pres. & CEO T.A. Lowrey, vice-chmn. & COO** *Includes \$1,057,991 paid in amended severance & noncompete agreements. **Resigned 4/29/97.	3298* 2075	59 1	1903 2669	15146 11979	118	4 4	26.4	-70.9	3 4
LEX	1618.8 14.8	F.A. Krehbiel, chmn. & CEO J.H. Krehbiel Jr., pres. & COO	967 851	4 13	95 45	3341 2832	183	1 2	12.9	37.3	1 2
TOROLA	29794.0 8.9	C.B. Galvin, CEO* G.L. Tooker, chmn. *Became CEO 1/1/97. **1997 long-term award has not yet been determined.	1951 1855	36 0	0** 0**	13409 16914	101	4 5	11.6	-48.2	4 4
CKWELL INTERNATIONAL	7888.0 11.3	D.R. Beall, chmn. & CEO D.H. Davis Jr., pres. & COO** *Includes \$1.25 mil. special bonus. Left company 7/3/97. **Became CEO 10/1/97.	3295 1543	10 11	1250* 0	10728 5231	192	3 3	14.7	-40.1	3 3
LECTRON	4023.5 17.5	K. Nishimura, chmn., pres. & CEO S. Zohouri, sr. v-p†	922 598	12 34	3335 723	5869 2176	302	1 1	16.2	4.3	2 1
AS INSTRUMENTS	9750.0 5.1	T.J. Engibous, pres. & CEO R.K. Templeton, exec. v-p†	2146 1459	321 423	0 0	6593 NA	248	2 NA	10.2	-77.5	5 NA

FOOD PROCESSING (CONSUMER PRODUCTS)

SHER DANIELS ISLAND	14697.4 7.0	D.O. Andreas, chmn. & CEO J.R. Randall, pres.†	4086 1968	5 5	0 0	11759 6434	125	4 4	10.6	-27.0	4 4
FTFOODS	8400.0 43.6	C.R. Shoemate, chmn., pres. & CEO A. Labergere, exec. v-p	1597 1086	9 39	3269 1884	15352 6939	215	3 3	32.7	121.6	2 1
MPBELL SOUP	8057.0 62.5	D.W. Johnson, chmn.* B.L. Anderson, exec. v-p & CFO† *Left office 7/15/97	1981 663	-8 183	1250 1502	10431 NA	280	3 NA	40.0	97.2	1 NA
AGRA	23828.5 25.5	P.B. Fletcher, chmn. & CEO B.C. Rohde, vice-chmn. & pres.	2507 1298	11 NA	3322 5382	14362 NA	226	3 NA	19.5	34.9	3 NA
IERAL MILLS	5788.4 100.2	S.W. Sanger, chmn. & CEO R.G. Viault, vice-chmn. *Includes \$192,000 deferred hiring bonus.	1062 1040*	-25 66	109 135*	3257 NA	168	1 NA	115.0	-45.6	1 NA
NZ (H.J.)	9180.0 16.0	A.J. O'Reilly, chmn. & CEO D.R. Williams, exec. v-p†	2405 993	-12 -5	0 530	68866 3339	228	5 1	17.6	-33.0	4 3
SHHEY FOODS	4302.2 39.4	K.L. Wolfe, chmn. & CEO J.P. Viviano, pres. & COO	1439 1140	3 11	2886 1322	9078 5758	272	2 2	29.7	208.4	2 1
LOGG	6830.1 56.5	A.G. Langbo, CEO T.A. Knowlton, exec. v-p	1646 770	32 17	3187 1314	11578 4539	183	3 3	42.9	44.9	2 1
ISCO HOLDINGS	8734.0 10.3	H.J. Greeniaus, chmn., pres. & CEO J.J. Postl, pres.-sub.* *Resigned 3/1/98.	1952 749	-1 -11	333 826	9038 4334	NA NA	NA NA	6.0	10.6	4 4
NEER HI-BRED INTERNATIONAL	1773.0 19.0	C.S. Johnson, chmn., pres. & CEO J.L. Chicoine, exec. v-p & CFO	1727 876	2 8	944 445	6442 3231	325	2 1	20.3	-21.5	3 2
KER OATS	5015.7 -409.8	W.D. Smithburg, chmn., pres. & CEO* J.F. Doyle, exec. v-p *Resigned 10/22/97. **Includes \$441,165 in special incentive award. ***Due to fiscal-year change in 1995, compensation for that year is for 18 months.	740 998	-16 36	278 1609**	5158*** 4396***	188	2 3	-106.3	-903.1	5 5
STON PURINA	4543.4 20.4	W.P. Stiritz, chmn., pres. & CEO J.W. Brown, v-p	2106 851	-2 63	4942 3968	15975 5806	220	3 3	42.6	-67.3	3 3
A LEE	19751.0 -25.0	J.H. Bryan, chmn. & CEO C.S. McMillan, pres.	2259 1311	-2 11	3523 2311	15319 7210	239	3 3	4.9	-515.6	5 5
CO	14779.4 22.7	B.M. Lindig, pres. & CEO J.F. Woodhouse, chmn. *Excludes portion of bonus paid in restricted stock.	1221* 1115*	16 7	497 456	4659 4536	186	2 3	19.8	29.8	2 2
ON FOODS	6348.6 11.2	L.E. Tollett, chmn. & CEO D. Tyson, chmn. *Includes \$703,676 related to travel & entertainment.	630 1422*	4 -16	0 0	2286 4815	147	1 3	10.6	NM	1 2
GLEY (WM.) JR.	1937.0 27.6	W. Wrigley, pres. & CEO D.S. Barrie, group v-p *1997 bonus & restricted stock awards not yet determined	500* 409*	-36 -34	25* 60*	3658 3484	170	2 2	27.1	-17.7	1 2

FOOD & LODGING (SERVICE)

ON HOTELS	5316.0 7.4	S.F. Bollenbach, pres. & CEO A.M. Goldberg, exec. v-p†	946 1000	-11 1633	0 0	NA NA	182	NA NA	8.7	-31.6	NA NA
ON GLOBAL TAURANTS	9681.0 NM	A.E. Pearson, chmn. & CEO D.C. Novak, vice-chmn. & pres.† *Includes \$850,000 one-time hiring bonus. Compensation paid from hire date of 7/1/97. Became CEO 10/21/97. **Compensation paid by PepsiCo prior to spin-off 10/97.	1881* 2376**	NA 148	0 0	NA NA	NA NA	NA NA	NM	NM	NA NA

GENERAL & SPECIAL MACHINERY (INDUSTRIAL: LOW TECH)

LIED MATERIALS	4546.2 22.5	J.C. Morgan, chmn. & CEO D. Maydan, pres.	1274 968	-19 -16	11376 12025	26534 25670	285	4 5	24.4	1.6	4 4
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re:
per

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abuses of the English language deserve to look their best.

MEMO

To: All Personnel
From: Bob

This is an FYI per request of the CEO (i.e. me) re routing of all memos. To recap, all memos must be OK'd by this office.

This policy is to be implemented ASAP. Please call me w/any questions. :-)

cc: dist
encl

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EXECUTIVE COMPENSATION SCOREBOARD

COMPANY	1997 SALES \$ MILLIONS ROE %	EXECUTIVE	1997 COMPENSATION			1995-97 PAY-PERFORMANCE ANALYSIS					
			TOTAL ANNUAL COMP SALARY & BONUS \$000	% CHANGE FROM 1996	LONG TERM COMP \$000	PAY VS. SHAREHOLDER RETURN			PAY VS. CORPORATE PROFIT		
						TOTAL COMP \$000	\$ VALUE OF \$100 INVESTED	RATING	ROE %	CHANGE IN ROE %	RATIN
BLACK & DECKER	4940.5	N.D. Archibald, chmn., pres. & CEO	2857	-45	1907	18722	171	5	12.7	11.6	4
	12.7	J. Galli, exec. v-p	1029	91	320	2786		2			2
CATERPILLAR	18925.0	D.V. Fites, chmn. & CEO	2530	10	1125	10048	187	3	34.1	8.5	2
	35.6	G.S. Flaherty, group pres.	884	15	375	5374		3			2
DANAHER	2051.0	G.M. Sherman, pres. & CEO	2133	39	0	19053	243	3	17.0	-1.6	4
	16.9	P.W. Allender, sr. v-p & CFO	621	17	0	1645		1			1
DEERE	13241.5	H.W. Becherer, chmn. & CEO	2264	7	2330	11732	280	2	23.2	0.9	3
	23.8	B.L. Hardiek, pres.†	846	9	410	3322		1			1
DOVER	4547.7	T.L. Reece, pres. & CEO	1675	3	1482	8951	292	2	24.2	17.1	2
	23.8	J.E. Pomeroy, v-p	860	11	1876	6941		2			3
INGERSOLL-RAND	7103.3	J.E. Perella, chmn., pres. & CEO	2122	19	593	7582	204	2	16.1	17.9	3
	16.3	J.F. Travis, vice-chmn.	1075	27	1155	4871		2			3
STANLEY WORKS	2669.5	J.M. Trani, chmn. & CEO	1700	NA	1640*	NA	285	NA	4.5	-140.9	NA
	-6.9	R.A. Hunter, pres. & COO**	618	0	1854	3614		2			5
*Joined company as CEO 1/1/97. Includes \$1.6 mil. for relocation expenses. **Resigned 1/3/98.											
TYCO INTERNATIONAL	NA	L.D. Kozlowski, chmn. & CEO	2857*	31	6521*	21593	385	3	NA	NA	NA
	NA	S.J. Ruzika, v-p & CFO†	3804**	113	10296***	16790		4			NA
†Data is from 7/2/97 to 9/30/97. **Compensation paid by ADT prior to merger. Compensation is for 9 mos. ***Includes \$2.7 mil. severance.											

16 INSTRUMENTS (INDUSTRIAL: HIGH TECH)

EMERSON ELECTRIC	12639.5	C.F. Knight, chmn. & CEO	2049	1	0	6132	194	2	19.5	-2.3	2
	20.3	A.E. Suter, sr. vice-chmn.	1000	0	0	2990		2			1
HONEYWELL	8027.5	M.R. Bonsignore, chmn. & CEO	2020	29	1907	8871	231	2	18.1	31.1	2
	19.7	G. Ferrari, pres. & COO	1207	NA	2265	NA		NA			NA

17 LEISURE TIME INDUSTRIES (CONSUMER PRODUCTS)

CARNIVAL	2447.5	M.M. Arison, chmn. & CEO	1694	40	1596	5715	271	2	18.8	-6.7	2
	18.5	H.S. Frank, vice-chmn. & COO	1308	46	1330	4473		2			3
DISNEY (WALT)	22534.0	M.D. Eisner, chmn. & CEO	10650	23	0	34071	219	4	13.0	-46.4	5
	10.8	S.M. Litvack, sr. exec. v-p	2225	27	0	9466		4			4
EASTMAN KODAK	14538.0	G.M. Fisher, chmn., pres. & CEO	2000	-46	15045*	35443	136	5	15.3	-98.9	5
	0.2	D.A. Carp, pres. & COO†	730	-35	39	5023		3			4
†Includes \$1.8 mil. loan forgiveness.											
HARLEY-DAVIDSON	1774.9	R.F. Teerlink, chmn.	1410	11	6321	10033	198	3	22.1	-8.2	3
	22.1	J.L. Bleustein, pres. & CEO*	1177	53	0	6333		3			3
*Became CEO 6/1/97											
MATTEL	4834.6	J.E. Barad, chmn. & CEO*	1546	-49	9140	23337	238	4	23.1	-33.7	4
	15.3	G.S. Baughman, pres.-sub.	1667**	NA	200	NA		NA			NA
*Became CEO 1/1/97. **Includes \$1.1 mil. signing bonus. Joined company 5/1/97											

18 METALS & MINING (RESOURCES)

ALUMINUM CO. OF AMERICA	13319.2	P.H. O'Neill, chmn. & CEO	2100	35	2713	23090	172	5	16.0	64.6	3
	18.4	A.J. Belda, pres. & COO	1460	37	8113	12299		5			4
NEWMONT MINING	1572.8	R.C. Cambre, chmn., pres. & CEO	1644	71	0	3824	84	3	8.8	-53.1	3
	4.3	W.W. Murdy, exec. v-p & CFO	685	66	67	2233		3			4
REYNOLDS METALS	6881.0	J.J. Sheehan, chmn. & CEO	1526	199	0	2980	131	1	8.1	0.1	2
	5.0	R.N. Reynolds, vice-chmn.	837	83	503	3059		3			3

19 MISCELLANEOUS MANUFACTURING (INDUSTRIAL: LOW TECH)

CORNING	4129.1	R.G. Ackerman, chmn. & CEO	2004	33	3768	12444	156	4	22.7	184.9	2
	35.2	V.C. Campbell, vice-chmn.	1461	23	3997	10746		5			3
FORTUNE BRANDS	4425.8	T.C. Hays, chmn. & CEO	3023*	28	2589	11816	165	3	9.5	-94.7	5
	1.0	J.T. Ludes, pres. & COO	1589**	20	702	5166		3			5
*Includes \$935,062 in tax reimbursement. **Includes \$421,266 in tax reimbursement.											
HILLENBRAND INDUSTRIES	1776.0	W.A. Hillenbrand, pres. & CEO	1504	6	0	3660	195	1	15.9	37.4	1
	17.7	T.E. Brewer, sr. v-p & CFO	515	6	0	1296		1			1
ILLINOIS TOOL WORKS	5220.4	W.J. Farrell, chmn. & CEO	1100	15	1621	4385	283	1	20.5	16.1	1
	20.9	F.S. Ptak, vice-chmn.	581	10	521	2269		1			1
JOHNSON CONTROLS	11440.4	J.H. Keyes, chmn. & CEO	1564	15	730	6369	209	1	14.2	1.2	3
	13.3	J.M. Barth, exec. v-p	859	22	1357	4850		2			3
MINNESOTA MINING & MFG.	15070.0	L.D. DeSimone, chmn. & CEO	1694	11	4986	13477	173	3	26.3	82.3	2
	35.8	R.A. Mitsch, vice-chmn. & exec. v-p	1041	11	1869	6418		3			2
NEWELL	3234.3	W.P. Sovey, vice-chmn. & CEO†	1376	7	906	4751	213	1	17.1	-2.5	2
	16.9	T.A. Ferguson Jr., pres. & COO	1040	8	206	3109		2			2
PARKER HANFIFIN	4360.3	D.E. Collins, pres. & CEO	1563	11	3318	9122	239	2	18.6	271.0	2
	20.0	D.W. Sullivan, exec. v-p	917	7	1513	5376		2			2
RUBBERMAID	2399.7	W.R. Schmitt, chmn. & CEO	719*	-47	782	5810	93	3	11.3	-23.5	3
	13.6	C.A. Carroll, pres. & COO	468*	-37	462	3321		3			3
*Excludes bonus paid in options.											



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EXECUTIVE COMPENSATION SCOREBOARD

COMPANY	EXECUTIVE		1997 COMPENSATION			1995-97 PAY-PERFORMANCE ANALYSIS				
	1997 SALES: \$ MILLIONS ROE		TOTAL ANNUAL SALARY & BONUS \$000	% CHANGE FROM 1996	LONG- TERM \$000	PAY VS. SHAREHOLDER RETURN TOTAL COMP. \$000	\$ VALUE OF \$100 INVESTED	RATING	PAY VS. CORPORATE PROFIT ROE %	CHANGE IN ROE %
20 NATURAL RESOURCES (RESOURCES)										
AMERADA HESS	8340.0 0.2	J.B. Hess, chmn. & CEO W.S. Laidlaw, pres. & COO	1200 1050	20 12	2738 2190	5838 5753	124 124	3 4	1.6	-90.5
AMOCO	31910.0 16.7	H.L. Fuller, chmn. & CEO W.G. Lowrie, pres.	1946 1229	2 4	1756 308	8263 3476	160 160	3 2	15.5	34.0
ASHLAND	13479.0 9.9	P.W. Chellgren, chmn. & CEO J.A. Brothers, exec. v-p	1738 862	57 11	2930 1300	7035 4779	169 169	2 3	7.6	-27.4
ATLANTIC RICHFIELD	18684.0 21.7	M.R. Bowlin, chmn. & CEO W.E. Wade Jr., pres.	2350 1115	15 11	907 967	7905 5084	180 180	2 3	21.1	49.0
BURLINGTON RESOURCES	2000.0 10.6	B.S. Shackouls, chmn., pres. & CEO H.L. Steward, vice-chmn.*	1538 696	26 NA	507 263	9785 NA	133 NA	4 NA	3.0	76.1
*Joined company 10/1/97										
CHEVRON	35009.0 18.6	K.T. Derr, chmn. & CEO J.N. Sullivan, vice-chmn.	2795 1476	19 21	7466 1413	17454 6756	192 192	4 4	13.9	60.7
COASTAL	9611.1 11.8	D.A. Arledge, chmn., pres., CEO O.S. Wyatt Jr., chmn.†	1123 593	11 -48	1035 24	5292 2915	248 248	1 1	12.4	35.0
EXXON	120279.0 19.3	L.R. Raymond, chmn. & CEO R.E. Wilhelm, sr. v-p	3276 1314	16 13	19273 4096	39751 11934	224 224	5 5	17.5	43.2
MOBIL	58399.0 16.8	L.A. Noto, chmn. & CEO E.A. Renna, exec. v-p	2064 1176	31 8	3564 2655	12363 9485	190 190	3 4	15.2	67.0
OCCIDENTAL PETROLEUM	8016.0 4.1	R.R. Irani, chmn. & CEO D.R. Laurance, pres.	3849 1907	-4 22	97657* 17327**	114557 22920	172 172	5 5	10.9	NM
*Includes \$95 mil. for restructuring of employment contract. **Includes \$17 mil. for restructuring of employment contract.										
PHILLIPS PETROLEUM	15210.0 19.9	W.W. Allen, chmn. & CEO J.J. Mulva, pres. & COO	1975 1364	1 3	568 1056	7913 5325	164 164	3 3	21.8	21.5
TEXACO	45187.0 21.0	P.I. Bijur, chmn. & CEO P.J. Lynch, sr. v-p & CFO†	1876 737	19 13	3666 1881	11286 4180	204 204	3 2	16.0	118.3
UNION PACIFIC RESOURCES GROUP	1905.7 18.9	J.L. Messman, chmn. & CEO G. Lindahl III, pres. & COO	2185 1149	39 57	464 124	9639 5267	NA NA	NA NA	22.3	-11.0
USX-MARATHON GROUP	12932.0 12.6	T.J. Usher, chmn. & CEO-USX Corp. V.G. Beghini, vice-chmn.	2418 1773	18 15	1441 58	9390 5720	227 227	2 3	9.9	26.6
21 NONBANK FINANCIAL (FINANCIAL SERVICES)										
AETNA	18540.2 8.2	R.E. Compton, chmn. & CEO† M.J. Cardillo, exec. v-p‡	1614 939	-38 -65	3709 83*	17693 7718	162 162	4 4	5.5	-3.6
*Excludes 25,752 stock options granted in 1998 in lieu of 1997 bonus.										
AFLAC	6983.5 20.9	D.P. Amos, pres. & CEO P.S. Amos, chmn.	2123 2374	1 3	19695 1734	31860 15163	248 248	5 4	18.6	25.3
AHMANSON (H.F.)	3649.9 15.9	C.R. Rinehart, chmn. & CEO B.G. Willison, pres. & COO	2743 1536	66 144	2733 1344	10682 NA	455 NA	2 NA	11.0	151.7
ALLSTATE	24949.0 20.3	J.D. Choate, chmn. & CEO E.M. Liddy, pres. & COO	2729 2612	131 160	3199 11907	9096 17005	403 403	2 4	16.9	253.5
AMERICAN EXPRESS	18958.0 20.8	H. Golub, chmn. & CEO K.I. Chenault, pres. & COO	3469 2255	11 30	29989 16919	51675 28398	319 319	5 5	20.8	-5.0
AMERICAN GENERAL	8927.0 7.5	R.M. Devlin, chmn. & CEO J.P. Newton, chmn.	2584 1133	89 58	2181 611	7243 2993	212 212	3 2	9.1	-49.5
AMERICAN INTERNATIONAL GROUP	27916.5 13.9	M.R. Greenberg, chmn. & CEO T.R. Tizio, sr. vice-chmn.	4650 1087	12 11	7362 1509	42998 8952	252 252	5 4	13.2	4.8
AON	5750.6 10.2	P.G. Ryan, chmn., pres. & CEO M.D. O'Halloran, pres. & COO-sub.‡	2022 1333	-27 -30	0 0	6572 6526	299 299	2 3	10.1	-30.2
ASSOCIATES FIRST CAPITAL	8278.6 16.5	K.W. Hughes, chmn. & CEO‡ H.D. Marshall, pres. & COO‡	1582 990	16 16	1100 690	10933 5418	NA NA	NA NA	16.8	-11.1
BEAR STEARNS	7090.7 20.2	J.E. Cayne, pres. & CEO A.C. Greenberg, chmn.	10376 14332	13 8	9616 4708	46192 44967	383 383	5 5	17.2	-3.8
BERKSHIRE HATHAWAY	9216.2 6.8	W.E. Buffett, chmn. & CEO M.D. Hamburg, v-p & CFO	100 281	0 10	198* 0	889 765	225 225	1 1	7.2	62.9
*Includes \$198,000 in director fees from a nonsubsidiary.										
CAPITAL ONE FINANCIAL	1787.1 21.2	R.D. Fairbank, chmn. & CEO‡ N.W. Morris, pres. & COO‡	676* 497*	6 14	0 0	1862 1307	349 349	1 1	21.1	5.6
†Elected to forgo bonus in exchange for stock option grants										
CHARTER ONE FINANCIAL	1491.7 11.0	C.J. Koch, chmn., pres. & CEO J.D. Koch, exec. v-p	808 501	6 3	5530 1379	7934 3280	394 394	2 1	9.6	-40.1
CHUBB	6652.0 13.6	D.R. O'Hare, chmn. & CEO J.J. Degnan, pres.	2424 928	15 25	1240 445	9973 3156	208 208	3 2	11.9	9.3
CIGNA	20038.0 13.6	W.H. Taylor, chmn. & CEO J.G. Stewart, exec. v-p & CFO	3270 1283	-7 9	9068 5979	28253 14278	294 294	4 4	10.4	42.6
CINCINNATI FINANCIAL	1942.4 6.3	R.B. Morgan, pres. & CEO J.J. Schiff Jr., chmn.	1257 642	12 12	3733 274	7249 2336	322 322	2 1	7.3	-38.8



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EXECUTIVE COMPENSATION SCOREBOARD

COMPANY	1997 SALES \$ MILLIONS ROE %	EXECUTIVE	1997 COMPENSATION			1995-97 PAY-PERFORMANCE ANALYSIS				
			TOTAL ANNUAL COMP SALARY & BONUS \$000	% CHANGE FROM 1996	LONG- TERM COMP \$000	PAY VS. SHAREHOLDER RETURN TOTAL COMP \$000	\$ VALUE OF \$100 INVESTED	RATING	PAY VS. CORPORATE PROFIT ROE %	CHANGE IN ROE %
CNA FINANCIAL	17072.0 12.3	D.H. Chookaszian, chmn. & CEO C.L. Murphy, sr. v-p	950 1080	0 18	1650 0	6593 2765	197 [2]	[3] [2]	12.5	1639.6
DONALDSON, LUFKIN & JENRETTE	4640.5 22.5	J.S. Chalsty, chmn. & CEO J.L. Roby, pres. & COO*† *Became CEO 2/23/98.	13155 9783	23 12	0 2548	41188 63686	NA NA	NA NA	18.2	80.5
DUN & BRADSTREET	2154.4 NM	V. Taylor, chmn. & CEO F.S. Sowinski, sr. v-p & CFO†	2148 702	47 44	171 20	7421 2008	164 [2]	[3] [2]	NM	NM
EQUIFAX	1366.1 53.1	D.W. McLaughlin, vice-chmn. & CEO† T.F. Chapman, pres. & COO *Excludes portion of bonus paid in restricted stock.	1261* 699*	1 -17	1878 1058	7922 4292	314 [2]	[3] [2]	45.6	59.7
EQUITABLE	9546.3 12.0	J.J. Melone, pres. & CEO† W.T. McCaffrey, exec. v-p†	3770 2069	23 27	1394 1244	11525 6368	281 [3]	[3] [3]	8.8	28.4
FRANKLIN RESOURCES	2358.0 23.6	C.B. Johnson, pres. & CEO M.L. Flanagan, sr. v-p & CFO	1032 1295	9 41	198 953	2953 6848	374 [3]	[1] [3]	23.1	-12.6
GENERAL RE	8253.2 11.7	R.E. Ferguson, chmn. & CEO J.E. Gustafson, pres. & COO *Excludes portion of bonus paid in restricted stock.	1893* 1100*	6 6	4065 3235	13649 8097	179 [4]	[4] [4]	12.0	-12.9
GOLDEN WEST FINANCIAL	2878.4 13.1	M.O. Sandler, co-chmn. & co-CEO H.M. Sandler, co-chmn. & co-CEO *Both executives hold the title of CEO.	1036 1031	6 5	9826 6256	16263 16893	283 [4]	[3] [4]	13.1	13.9
GREEN TREE FINANCIAL	1707.7 22.6	L.M. Coss, chmn. & CEO R.D. Potts, pres. & COO** *As reported in the company's proxy statement. May be restated in 1999. **Resigned 12/15/97.	4837 2078	-95 27	6426 0	179291* 4894	177 [3]	[5] [3]	22.6	-9.4
HARTFORD FINANCIAL SERVICES GROUP	13305.0 22.9	R. Ayer, chmn., pres. & CEO* L.A. Smith, vice-chmn. *Became CEO 2/1/97.	1199 1012	45 21	5025 3003	9898 7006	NA NA	NA NA	10.9	15.5
HARTFORD LIFE	4699.0 14.3	L.A. Smith, pres. & CEO*† T.M. Marra, exec. v-p† *Became CEO 5/1/97.	1012 1016	21 6	3003 1142	NA NA	NA NA	NA NA	9.6	NA
HOUSEHOLD INTERNATIONAL	5453.1 15.6	W.F. Aldinger, chmn. & CEO R.F. Elliott, vice-chmn.	2480 870	6 -3	0 765	6683 4082	364 [2]	[2] [2]	16.4	1.5
JEFFERSON-PILOT	2578.1 14.2	D.A. Stonecipher, pres. & CEO K.C. Mlekush, exec. v-p	1866 650	26 15	540 180	6069 2219	244 [2]	[3] [2]	12.9	6.8
LEHMAN BROTHERS HOLDINGS	16883.0 14.2	R.S. Fuld Jr., chmn. & CEO J.L. Cecil, chief administrative officer	3875 3750	41 56	5961 3215	21571 15091	354 [4]	[4] [4]	10.7	335.0
LOEWS	19772.6 8.5	L.A. Tisch, co-chmn. & co-CEO P.R. Tisch, co-chmn. & co-CEO	2115 2559	16 14	26 26	4883 7045	252 [3]	[2] [3]	15.3	72.2
MARSH & McLENNAN	6008.6 12.0	A.J. Smith, chmn. & CEO L.J. Lasser, pres.-Putnam Invest.	2334 12870	-4 24	2057 24585	12624 59709	208 [5]	[3] [5]	20.2	-54.1
MBIA	654.0 12.3	D.H. Elliott, chmn. & CEO R.L. Weill, vice-chmn. *Excludes \$600,025 bonus paid in restricted stock. **Excludes \$366,639 bonus paid in restricted stock.	1037* 645**	20 7	2223 1204	9917 4156	250 [3]	[3] [3]	12.5	-19.6
MERRILL LYNCH	31731.0 23.6	D.H. Komansky, chmn. & CEO H.M. Allison Jr., pres. & COO	7729 6140	36 33	15923 10947	35588 26638	430 [4]	[4] [4]	22.9	19.8
MGIC INVESTMENT	871.3 21.8	W.H. Lacy, pres. & CEO C.S. Culver, exec. v-p	1088 635	21 23	0 1762	7630 4943	405 [2]	[2] [2]	19.7	14.4
MORGAN STANLEY DEAN WITTER	27132.0 19.2	P.J. Purcell, chmn. & CEO*† J.J. Mack, pres. & COO *Became CEO 5/31/97. **Payment received upon exercise of options. Compensation paid by Dean Witter prior to merger 5/97.	11274** 10474	241 66	39533 4163	58683 42514	364 [5]	[5] [5]	16.4	122.8
OLD REPUBLIC INTERNATIONAL	1962.8 14.1	A.C. Zucaro, pres. & CEO W.A. Simpson, sr. v-p	1203 759	-4 3	0 0	3547 2307	276 [1]	[1] [1]	12.9	29.9
PAINWEBBER GROUP	6657.0 22.0	D.B. Marron, chmn. & CEO J.J. Grano Jr., pres.	8463 5713	21 4	2788 5462	39198 22849	367 [4]	[4] [4]	15.4	1005.4
PRICE (T. ROWE) ASSOCIATES	755.0 29.7	G.A. Roche, chmn. & pres.* M.D. Testa, vice-chmn. *Became CEO 4/17/97.	2525 2525	42 42	554 229	7284 7039	436 [1]	[1] [3]	28.7	4.9
PROGRESSIVE	4608.2 19.4	P.B. Lewis, chmn., pres. & CEO C.B. Chokel, treas. & CFO	2922 1218	29 49	0 2941	7205 6211	347 [2]	[2] [3]	18.4	-22.3
RELIASTAR FINANCIAL	2510.3 11.0	J.G. Turner, chmn. & CEO J.H. Flittie, pres. & COO	1114 762	-1 0	1692 1484	7390 5835	304 [2]	[2] [3]	12.0	-18.1
SAFECO	4709.3 7.9	R.H. Eigsti, chmn. & CEO B.A. Dickey, pres. & COO	902 605	23 21	597 580	4324 2874	204 [2]	[2] [2]	9.5	-29.1
SCHWAB (CHARLES)	2845.3 25.1	C.R. Schwab, chmn. & CEO D.S. Pottruck, pres. & COO* *Became co-CEO 1/1/98.	7162 5014	-30 -30	0 0	26756 25719	552 [3]	[3] [4]	26.6	-13.5
ST. PAUL	6219.3 17.3	D.W. Leatherdale, chmn., pres. & CEO P.J. Liska, exec. v-p & CFO *Received \$236,507 related to relocation expenses.	1318 1676	33 NA	465 1182*	4555 NA	200 NA	[2] NA	14.9	8.6
SUNAMERICA	1225.2 16.4	E. Broad, pres. & CEO M. Fowler, v-p	3505 4162	16 42	6236 760	28563 11568	547 [3]	[3] [3]	18.1	-24.4



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EXECUTIVE COMPENSATION SCOREBOARD

COMPANY	1997 SALES \$ MILLIONS ROE: %	EXECUTIVE	1997 COMPENSATION			1995-97 PAY-PERFORMANCE ANALYSIS				
			TOTAL ANNUAL COMP SALARY & BONUS \$000	% CHANGE FROM 1996	LONG- TERM COMP \$000	PAY VS. SHAREHOLDER RETURN TOTAL COMP \$000	\$ VALUE OF \$100 INVESTED	RATING	PAY VS. CORPORATE PROFIT ROE %	CHANGE IN ROE %
TORCHMARK	2282.5	R.K. Richey, chmn. & CEO	1188	-20	11571*	16090	259	4	17.9	-21.7
	16.9	C.B. Hudson, chmn. & CEO-sub. *Excludes portion of bonus paid in options for 1998.	1200	44	19236*	22383		5		
TRANSAMERICA	5726.5	F.C. Herringer, chmn., pres. & CEO	1950	13	18093	25773	232	4	11.2	-33.8
	10.8	R.A. Watson, exec. v-p†	1050	12	0	2497		2		
TRAVELERS GROUP	37609.0	S.I. Weill, chmn. & CEO	7453	18	223272	374722	522	5	15.7	-3.6
	15.3	J. Dimon, pres. & COO	5255	17	39005	73532		5		
TRAVELERS PROPERTY CASUALTY	9910.9	R.I. Lipp, chmn., pres. & CEO†	3730	13	22570	43585	NA	NA	11.5	NA
	17.0	J.S. Fishman, vice-chmn.†	1533	23	4620	11352		NA		
UNUM	4004.1	J.F. Orr III, chmn. & CEO	1980	34	3849	9609	304	3	12.6	88.3
	15.2	R.W. Crispin, exec. v-p	865	0	907	5414		3		
WASHINGTON MUTUAL	7446.5	K.K. Killinger, chmn., pres. & CEO	1409	51	0	3360	410	1	7.9	-24.7
	8.9	C.E. Tall, exec. v-p	531	36	0	1330		1		
22 OFFICE EQUIPMENT & COMPUTERS (INDUSTRIAL: HIGH TECH)										
AMERICA ONLINE	2039.5	S.M. Case, chmn., pres. & CEO	271	36	26642	57431	646	3	-0.7	21.8
	7.7	B.R. Bond, pres.-sub.	513	NA	0	NA		NA		
AUTOMATIC DATA PROCESSING	4392.4	A.F. Weinbach, pres. & CEO	887	25	1729	6312	216	2	18.8	-9.0
	18.0	G.C. Butler, group pres.	698	8	1897	5177		3		
BAY NETWORKS	2302.1	D.L. House, chmn., pres. & CEO	1323	NA	0	NA	130	NA	11.8	-103.6
	-1.2	D.A. Shrigley, exec. v-p	602	NA	0	NA		NA		
CADENCE DESIGN SYSTEMS	915.9	J.B. Costello, pres. & CEO*	584	-60	66258	69669	535	3	34.8	20.1
	25.0	J.F. Olsen, exec. v-p *Left office 10/18/97.	941	40	4692	9545		2		
CERIDIAN	1074.8	L. Perlman, chmn., pres. & CEO	1200	-16	3181	19465	170	4	37.6	-83.3
	6.0	R.L. Turner, exec. v-p	664	12	0	2522		2		
CISCO SYSTEMS	7298.0	J.T. Chambers, pres. & CEO	558	-10	0	42654	476	3	29.1	-34.4
	24.4	L.R. Carter, v-p†	493	0	0	4118		1		
COMPAQ COMPUTER	24584.0	E. Pfeiffer, pres. & CEO	4500	6	0	48414	358	4	19.4	-16.6
	19.7	R. Pieper, sr. v-p	1787	NA	15809*	NA		NA		
*Includes stock options granted by Tandem converted into Compaq options. Joined company 9/1/97 and resigned 1/1/98.										
COMPUTER ASSOCIATES INTERNATIONAL	4457.0	C.B. Wang, chmn. & CEO	6000	0	11589	37255	371	3	24.2	89.8
	52.0	S. Kumar, pres. & COO	4150	6	6552	35462		4		
COMPUWARE	1034.1	P. Karmanos Jr., chmn. & CEO	1830	187	0	3090	356	1	20.8	44.6
	26.7	J.A. Nathan, pres. & COO	1464	175	763	5732		2		
DIGITAL EQUIPMENT	13062.2	R.B. Palmer, chmn., pres. & CEO	1002	11	0	3942	112	2	1.2	NM
	7.1	B.L. Claflin, sr. v-p	815	NA	419	NA		NA		
ELECTRONIC DATA SYSTEMS	15235.6	L.M. Alberthal Jr., chmn. & CEO†	869	-55	12919	24165	119	5	13.9	-29.1
	13.8	J.M. Heller, pres. & COO†	515	-50	10766	13267		4		
EMC	2937.9	M.C. Ruettgers, pres. & CEO	1613	52	2184	15797	249	3	25.0	-34.2
	22.7	M.A. Klayko, sr. v-p	1509	217	281	NA		NA		
FIRST DATA	5234.5	H.C. Duques, chmn. & CEO	600	-2	1727	6756	124	3	8.1	-52.4
	9.8	C.T. Fote, exec. v-p	661	27	643	2279		2		
HBO & CO.	1203.2	C.W. McCall, pres. & CEO	1725	10	49684	84900	562	4	7.4	-48.2
	15.9	J.P. Gilbertson, pres. & co-COO	626	48	4390	8648		2		
HEWLETT-PACKARD	44416.0	L.E. Platt, chmn., pres. & CEO	1811	-1	8052	20198	257	3	19.6	18.8
	19.1	R.P. Wayman, exec. v-p & CFO	1032	10	5594	12493		3		
IBM	78508.0	L.V. Gerstner Jr., chmn. & CEO	6000	26	8799	38358	293	4	25.0	136.0
	31.0	J.M. Thompson, sr. v-p	1400	21	10503	22914		4		
MICROSOFT	13098.0	W.H. Gates III, chmn. & CEO	591	5	0	1570	423	1	31.0	32.1
	34.0	R.J. Herbold, exec. v-p & COO *Includes \$250,000 payment related to joining company.	1209*	12	0	3123		1		
ORACLE	6303.2	L.J. Ellison, chmn. & CEO	2850	22	0	36067	171	5	31.4	-25.5
	27.2	R.J. Lane, pres. & COO	2278	49	6743	37001		5		
PARAMETRIC TECHNOLOGY	848.3	S.C. Walske, chmn. & CEO	730	-29	10328	37941	275	4	26.6	15.9
	32.0	C.R. Harrison, pres. & COO	675	-31	9863	25419		4		
PITNEY BOWES	4100.5	M.J. Critelli, chmn. & CEO	1794	36	1446	6999	307	1	22.9	40.7
	28.1	M.C. Breslawsky, pres. & COO	1496	16	2106	7334		3		
SABRE GROUP HOLDINGS	1783.1	M.J. Durham, pres. & CEO†	714	15	636	3812	NA	NA	NA	NA
	26.5	T.M. Cook, sr. v-p†	373	7	308	1786		NA		
SEAGATE TECHNOLOGY	8047.9	A.F. Shugart, chmn. & CEO	1937	35	0	24581	160	4	7.3	-121.2
	-3.6	S.J. Luczo, pres. & COO†	1486	39	3748	11173		4		
STERLING COMMERCE	382.1	W.C. Blow, pres. & CEO	958	22	0	5056		NA	44.4	NA
	10.1	S.L. Williams, chmn.	900	80	0	8540		NA		
SUN MICROSYSTEMS	9206.6	S.G. McNealy, chmn., pres. & CEO	2567	12	14974	28763	449	3	20.6	97.4
	23.7	E.J. Zander, pres.-sub.	1080	35	2780	10321		2		
3COM	5763.6	E.A. Benhamou, pres. & CEO	688	10	11993	30912	136	5	18.3	-55.4
	12.1	R.J. Finocchio Jr., pres.-sub.* *Resigned 5/1/97.	453	8	8729	21975		5		

A woman with short brown hair, wearing a black blazer over a white top, is seated at a desk in a busy office. She is smiling and talking on a black mobile phone held to her ear. In the foreground, a white sign with red and black text reads "TIL THE YEAR 2000 FRIDAYS FREE". The background is filled with office equipment, including computer monitors, papers, and other workers, creating a sense of a fast-paced environment.

A white cake shaped like a calendar page, sitting on a black base. The cake has text printed on it: "TIL THE YEAR 2000" in a small black box, "FRIDAYS" in large red letters, and "FREE" in large black letters with a thick black underline. The cake is decorated with white frosting and has a small white tag attached to the top.

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EXECUTIVE COMPENSATION SCOREBOARD

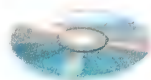
COMPANY	1997 SALES \$ MILLIONS ROE %	EXECUTIVE	1997 COMPENSATION			1995-97 PAY-PERFORMANCE ANALYSIS					
			TOTAL ANNUAL COMP SALARY & BONUS \$000	% CHANGE FROM 1996	LONG- TERM COMP \$000	PAY VS. SHAREHOLDER RETURN			PAY VS. CORPORATE PROFIT		
						TOTAL COMP \$000	\$ VALUE OF \$100 INVESTED	RATING	ROE %	CHANGE IN ROE %	RATING
23 OIL SERVICE & SUPPLY (RESOURCES)											
BAKER HUGHES	3992.1	M.L. Lukens, chmn., pres. & CEO	1664	44	0	6218	251	1	7.7	-28.6	3
	5.2	E.L. Mattson, pres. & CFO	732	19	128	2655		1			3
DIAMOND OFFSHORE DRILLING	956.1	R.E. Rose, pres. & CEO	601*	-5	0	1853	NA	NA	9.7	NM	1
	18.1	L.R. Dickerson, sr. v-p & CFO	447	33	0	1079		NA			1
*Bonus forfeited because of resignation. Resigned 3/31/98.											
DRESSER INDUSTRIES	7437.9	W.E. Bradford, chmn. & CEO	1879	34	1535	5936	239	2	16.2	-11.7	2
	19.6	D.C. Vaughn, pres. & COO	1197	40	538	3496		2			2
GLOBAL MARINE	1067.1	C.R. Luigs, chmn. & CEO	1047	40	2494	7813	678	1	32.5	1630.0	1
	39.1	J.G. Ryan, pres. & COO	514	25	8506	13566		2			2
HALLIBURTON	8818.6	R.B. Cheney, chmn. & CEO	3080	45	0	9780	344	2	15.0	92.0	2
	17.6	D.J. Lesar, pres. & COO†	1150	23	3869	8335		3			3
SCHLUMBERGER	10647.6	D.E. Baird, chmn. & CEO	3000	36	12225	31063	336	4	15.9	65.5	4
	19.4	V.E. Grijalva, exec. v-p	1050	2	2982	7679		3			3
24 PAPER & FOREST PRODUCTS (RESOURCES)											
FORT JAMES	7259.0	M.L. Marsh, chmn. & CEO	2676	15	5520	16437	213	4	12.4	NM	2
	26.4	M.T. Riordan, pres. & COO†	1817	96	6941	11043		4			2
GEORGIA-PACIFIC	12968.0	A.D. Correll, chmn., pres. & CEO	2138*	70	0	5864	130	3	10.4	-119.0	5
	-2.4	J.F. McGovern, exec. v-p	864	53	0	2166		2			5
*Includes \$1.1 mil. for taxes on vested restricted stock.											
INTERNATIONAL PAPER	20115.0	J.T. Dillon, CEO	1713	140	2995	11963	123	4	5.4	-126.0	5
	-1.7	C.W. Smith, exec. v-p	775	80	1217	4274		4			5
KIMBERLY-CLARK	12546.6	W.R. Sanders, chmn. & CEO	1186	-30	6751	17279	215	4	17.9	4.0	3
	21.4	K.P. Seifert, group pres.†	572	-11	370	2358		1			1
UNION CAMP	4476.8	W.C. McClelland, chmn. & CEO	1081	40	818	4358	126	2	9.8	-38.2	3
	3.9	J.H. Ballengee, pres. & COO	683	33	184	2592		2			3
WEYERHAEUSER	11210.0	J.W. Creighton Jr., pres. & CEO*	989	-21	2377	7466	145	3	11.7	-46.4	4
	7.4	R.C. Gozon, exec. v-p	450	-16	0	1712		1			3
*Left office 12/1/97.											
WILLAMETTE INDUSTRIES	3438.7	S.R. Rogel, pres. & CEO*	769	-2	2452	4893	144	2	13.8	-71.4	3
	3.7	W.P. Kinnune, exec. v-p	458	7	0	2336		2			3
*Resigned 11/1/97.											
25 PERSONAL-CARE PRODUCTS (CONSUMER PRODUCTS)											
AVON PRODUCTS	5079.4	J.E. Preston, chmn. & CEO	1424	22	5491	13772	222	3	133.0	-16.7	1
	118.9	F. Lezama, exec. v-p	634	NA	654	NA		NA			NA
CLOROX	2652.7	G.C. Sullivan, chmn. & CEO	1655	33	1069	5766	291	2	23.9	33.8	2
	26.5	W.F. Ausfahl, group v-p & CFO	657	25	1484	4298		2			2
COLGATE-PALMOLIVE	9056.7	R. Mark, chmn. & CEO	3847	44	21544	46979	248	5	24.3	7.3	4
	33.3	W.S. Shanahan, pres. & COO	2259	43	16742	23461		5			4
ESTEE LAUDER	3468.8	L.A. Lauder, chmn. & CEO†	4454	35	0	10064	NA	NA	29.7	NA	NA
	30.5	F.H. Langhammer, pres. & COO†	3150	5	1500	13601		NA			NA
GILLETTE	10062.0	A.M. Zeien, chmn. & CEO	3417	15	5311	20657	278	3	28.2	-15.5	3
	29.9	M.C. Hawley, pres. & COO	1358	19	0	5659		2			2
PROCTER & GAMBLE	36715.0	J.E. Pepper, chmn. & CEO	1180*	6	1661	8891	272	2	26.5	21.8	2
	29.6	D.I. Jager, pres. & COO	1035**	7	1278	5361		2			2
*Excludes bonus paid in restricted stock & options granted in 1997. **Excludes portion of bonus paid in options in 1997.											
26 PUBLISHING, RADIO & TV BROADCAST (SERVICE)											
CBS	5363.0	M.H. Jordan, chmn. & CEO	3058	53	86	7917	249	3	-6.9	-225.7	5
	-1.9	L. Moonves, pres.-sub.†	4154	4	0	8301		3			4
CLEAR CHANNEL COMMUNICATIONS	697.1	L.L. Mays, chmn. & CEO	2726	5	4482	11908	626	2	10.2	-77.8	4
	3.7	M.P. Mays, pres. & COO†	732	112	4616	5864		2			4
COX COMMUNICATIONS	1610.4	J.O. Robbins, pres. & CEO	642*	7	353	4092	NA	NA	-1.2	-282.0	5
	-5.8	A.M. Dalvi, sr. v-p	420	4	500	2059		NA			5
*Excludes bonus paid in restricted stock.											
DOW JONES	2572.5	P.R. Kann, chmn. & CEO	925	-16	304	4232	187	2	-26.4	-940.1	5
	-102.7	K.L. Burenga, pres. & COO	730	-11	190	3145		2			5
GANNETT	4729.5	J.J. Curley, chmn. & CEO	2155	23	3867	13092	246	3	21.3	-19.8	3
	20.5	D.H. McCorkindale, vice-chmn. & pres.	1937	26	1161	7568		3			3
KNIGHT-RIDDER	2876.8	P.A. Ridder, chmn., pres. & CEO	1535	9	1917	6687	219	3	21.4	83.3	4
	25.6	R. Jones, sr. v-p	767	16	0	1940		1			1
MCGRAW-HILL	3534.1	J.L. Dionne, chmn. & CEO†	2398	25	12419	21210	241	4	26.2	-8.9	5
	20.3	H.W. McGraw III, pres. & COO*	1422	21	1406	6525		3			5
*Will become CEO 4/29/98.											
NEW YORK TIMES	2866.4	A.O. Sulzberger, chmn. emeritus	1423	2	4772	9254	315	3	9.6	9.8	4
	15.2	R.T. Lewis, pres. & CEO*	1163	30	1868	NA		NA			N
*Became CEO 10/16/97.											

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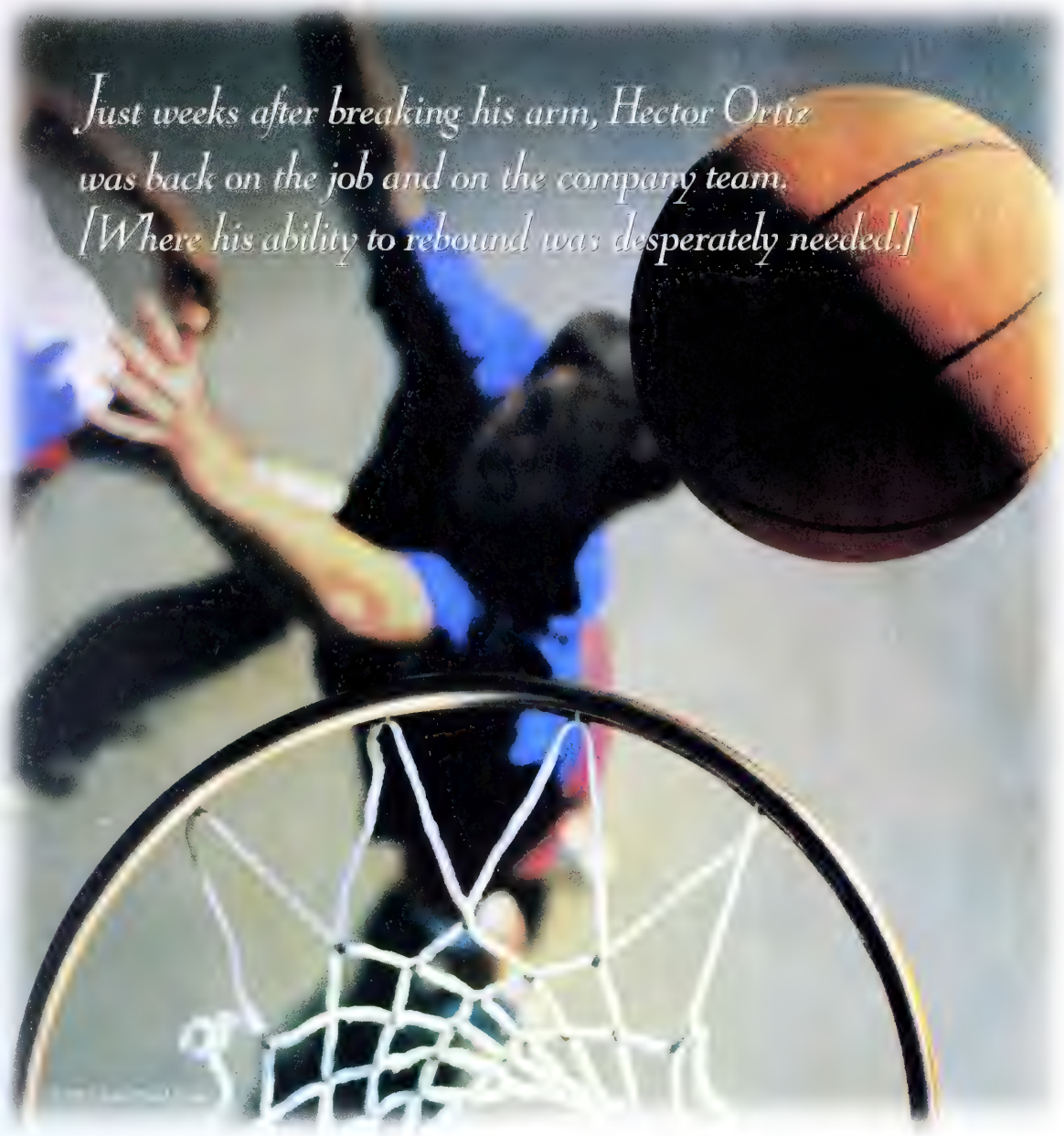
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EXECUTIVE COMPENSATION SCOREBOARD

COMPANY	EXECUTIVE	1997 COMPENSATION			1995-97 PAY-PERFORMANCE ANALYSIS					
		TOTAL ANNUAL COMP. SALARY & BONUS \$000	% CHANGE FROM 1996	LONG- TERM COMP. \$000	PAY VS. SHAREHOLDER RETURN			PAY VS. CORPORATE PROFIT		
	1997 SALES \$ MILLIONS ROE %				TOTAL COMP. \$000	\$ VALUE OF \$100 INVESTED	RATING	ROE %	CHANGE IN ROE %	RATIN
SCRIPPS (E.W.)	1242.0 15.3	W.R. Burleigh, pres. & CEO P.F. Gardner, sr. v-p	1004 613	15 9	310 345	4185 2299	261 [2] [1]	12.3	34.8	[2] [2]
TIME WARNER	13294.0 -0.2	G.M. Levin, chmn. & CEO R.E. Turner, vice-chmn.	7749 6050	47 390	1689 0	20904 NA	181 [4] NA	-3.1	NM	[4] NA
TIMES MIRROR	3318.5 144.1	M.H. Willes, chmn., pres. & CEO T. Unterman, exec. v-p & CFO	2884 1024	34 20	557 127	9388 3310	297 [3] [2]	42.4	2133.9	[1] [1]
TRIBUNE	2719.8 22.0	J.W. Madigan, chmn., pres. & CEO J.C. Dowdle, exec. v-p	1885 1158	30 24	7514 6400	17905 14936	239 [3] [5]	19.3	24.1	[3] [3]
WASHINGTON POST	1956.3 20.4	D.E. Graham, CEO A.G. Spoon, pres. & COO	400 960	0 13	1020 5031	2804 8305	210 [1] [4]	17.7	35.7	[1] [3]
27 RAILROADS (TRANSPORTATION)										
BURLINGTON NORTHERN SANTA FE	8413.0 13.0	R.D. Krebs, chmn., pres. & CEO D.G. McInnes, sr. v-p	559* 626*	0 -4	5840 973	19751 6816	202 [4] [5]	10.5	-38.9	[4] [4]
*Excludes portion of bonus paid in restricted stock.										
CSX	10621.0 13.9	J.W. Snow, chmn., pres. & CEO G.L. Nichols, vice-chmn.†	1246* 922	-4 16	6567 963	18273 4744	166 [5] [3]	15.2	-20.7	[3] [3]
*Excludes portion of bonus paid in restricted stock.										
KANSAS CITY SOUTHERN INDUSTRIES	1058.3 -2.0	L.H. Rowland, chmn., pres. & CEO T.H. Bailey, chmn. & CEO-sub.	808 1575	46 60	0 60	6667 3210	316 [2] [2]	17.9	-112.9	[3] [3]
NORFOLK SOUTHERN	4943.1 13.9	D.R. Goode, chmn., pres. & CEO H.C. Wolf, exec. v-p	1988 851	-38 -24	2473 848	13761 4467	164 [4] [3]	14.7	-2.4	[2] [2]
UNION PACIFIC	11079.0 5.3	R.K. Davidson, chmn. & CEO J.R. Davis, pres. & COO†	901 600	-52 -48	529 400	4961 3812	214 [2] [3]	8.0	-71.9	[5] [5]
28 RETAILING: FOOD (SERVICE)										
ALBERTSON'S	14689.5 21.4	G.G. Michael, chmn. & CEO R.L. King, pres. & COO	1101 645	1 15	1395 435	6110 1978	171 [3] [2]	22.4	-13.6	[2] [1]
May contain data from a preliminary source.										
KROGER	26567.3 NM	J.A. Pichler, chmn. & CEO D.B. Dillon, pres. & COO	875 612	-9 -6	2435 1021	5345 4526	305 [2] [2]	NM	NM	NA NA
May contain data from a preliminary source.										
SAFEWAY	22483.8 28.9	S.A. Burd, pres. & CEO K.W. Oder, exec. v-p	1318* 776*	-3 -9	12977 4728	20880 7194	397 [3] [3]	36.3	-25.6	[3] [2]
May contain data from a preliminary source. *Salary reflects 53-week pay period.										
WINN-DIXIE STORES	13382.3 15.7	A.D. Davis, chmn. & CEO J. Kufeldt, pres.	603 603	-20 -20	0 326	2075 3029	185 [1] [2]	17.8	-23.4	[2] [2]
29 RETAILING: NONFOOD (SERVICE)										
AUTOZONE	2797.6 18.1	J.C. Adams Jr., chmn. & CEO** T.D. Vargo, pres. & COO†	613 528	59 38	0 0	1200 1060	120 [1] [1]	19.2	-17.9	[1] [1]
*Became CEO 12/31/96.										
CARDINAL HEALTH	11616.6 15.1	R.D. Walter, chmn. & CEO J.C. Kane, pres. & COO	1355 880	46 25	650 217	3877 2530	244 [2] [2]	14.2	63.7	[2] [2]
COSTCO	22420.8 14.7	J.D. Sinegal, pres. & CEO J.H. Brotman, chmn.	500 500	11 11	0 0	1256 1256	347 [1] [1]	14.3	123.7	[1] [1]
CVS	12738.2 1.2	S.P. Goldstein, chmn. & CEO T.M. Ryan, vice-chmn. & COO†	2575 1753	26 -44	1243 1778	7383 9275	257 [2] [4]	-5.5	-90.1	[5] [5]
GAP	6507.8 33.7	M.S. Drexler, pres. & CEO R.J. Fisher, exec. v-p	3736 1762	14 13	0 0	10814 5235	359 [3] [2]	27.6	44.7	[2] [2]
May contain data from a preliminary source.										
RITE AID	10841.6 8.9	M.L. Grass, chmn. & CEO T.J. Noonan, pres. & COO	1900 1330	19 66	0 0	7642 3715	269 [2] [2]	9.9	-36.0	[3] [3]
SEARS, ROEBUCK	41296.0 20.3	A.C. Martinez, chmn., pres. & CEO R.L. Mettler, pres.-sub.	1515 946	-56 -39	771 2044	10930 7719	204 [3] [4]	23.3	54.1	[2] [2]
WALGREEN	13794.0 18.5	C.R. Walgreen III, chmn. & CEO L.D. Jorndt, pres. & COO	1755 1210	18 20	9173 2761	14812 6719	299 [3] [3]	18.2	3.0	[3] [3]
30 SERVICE INDUSTRIES (SERVICE)										
BROWNING-FERRIS INDUSTRIES	5632.6 14.7	B.E. Ranck, pres. & CEO N.A. Myers, exec. v-p	727* 635**	21 25	158 53	2494 2670	139 [2] [3]	8.4	23.6	[2] [2]
*Excludes 50% of bonus paid in restricted stock. **Excludes 25% of bonus paid in restricted stock.										
CENDANT	3593.0 -4.7	W.A. Forbes, chmn. & CEO C.K. McLeod, vice-chmn.	1563 1035	3 8	7790* 16000**	38194 38818	233 [5] [5]	10.3	-117.7	[2] [2]
*Includes \$7.5 mil. in retirement benefits related to merger. Left office 12/17/97. **Includes \$7.4 mil. in retirement benefits related to merger.										
CINTAS	926.1 17.8	R.J. Kohlhepp, pres. & CEO R.T. Farmer, chmn.	483 524	9 -4	0 0	1584 3542	223 [1] [2]	17.7	3.5	[1] [1]
COGNIZANT	1418.2 39.0	R.E. Weissman, chmn. & CEO† W.G. Jacobi, exec. v-p†	1758 780	-38 -27	470 136	12483 4069	NA NA NA	25.4	NA	NA NA
COLUMBIA/HCA HEALTHCARE	18819.0 2.1	R.L. Scott, chmn. & CEO* D.E. Steen, pres.**	548 634	-40 11	5154 1673	9738 3741	123 [4] [3]	11.5	-86.2	[1] [1]
May contain data from a preliminary source. *Resigned 7/25/97. **Left company 12/31/97.										



Just weeks after breaking his arm, Hector Ortiz was back on the job and on the company team. [Where his ability to rebound was desperately needed.]

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EXECUTIVE COMPENSATION SCOREBOARD

COMPANY	1997 SALES \$ MILLIONS ROE %	EXECUTIVE	1997 COMPENSATION			1995-97 PAY-PERFORMANCE ANALYSIS					
			TOTAL ANNUAL COMP. SALARY & BONUS \$000	% CHANGE FROM 1996	LONG- TERM COMP \$000	PAY VS. SHAREHOLDER RETURN			PAY VS. CORPORATE PROFIT		
						TOTAL COMP. \$000	\$ VALUE OF \$100 INVESTED	RATING	ROE %	CHANGE IN ROE %	RATING
DONNELLEY (R.R.) & SONS	4850.0 13.0	W.L. Davis, chmn. & CEO J.P. Ward, pres. & COO	1246 868	NA 96	13628* 170	NA 3258	134 NA	NA [3]	5.7	-4.4	NA [3]
*Includes \$3.9 mil. signing bonus. Joined company 1/1/97 and became CEO 3/1/97.											
ENRON	20373.0 1.8	K.L. Lay, chmn. & CEO J.K. Skilling, chmn. & COO†	1904 1223	-31 -1	1438 10230	18472 21774	146 NA	[4] [5]	11.4	-88.9	[4] [4]
FDX	12571.4 13.9	F.W. Smith, chmn., pres. & CEO T.L. Weise, exec. v-p	1239 1332*	41 -9	1125 3135	5754 8382	203 NA	[2] [4]	12.7	4.8	[3] [3]
*Includes \$614,545 tax reimbursement											
FLUOR	14263.5 8.0	L.G. McCraw, chmn. & CEO† D.L. Blankenship, chmn. & CEO-sub.	1102 910	-46 12	2003 354	8762 3498	90 NA	[4] [4]	13.4	-49.4	[3] [3]
GENUINE PARTS	6005.2 18.4	L.L. Prince, chmn. & CEO T.C. Gallagher, pres. & COO	1199 842	7 7	2479 1240	7014 4348	155 NA	[3] [3]	18.7	-2.6	[2] [2]
GRAINGER (W.W.)	4136.6 17.9	R.L. Keyser, chmn. & CEO J.D. Fluno, vice-chmn.	1145 932	-2 -5	445 0	8148 7726	175 NA	[3] [4]	16.0	44.6	[2] [3]
HEALTH MANAGEMENT ASSOCIATES	930.9 19.2	W.J. Schoen, chmn. & CEO J.V. Vumbacco, pres. & COO	1041 557	5 100	29905 261	45541 NA	341 NA	[5] NA	19.8	-1.0	[3] NA
HEALTHSOUTH	3017.3 17.1	R.M. Scrushy, chmn. & CEO M.D. Martin, exec. v-p & CFO	13399 2360	18 129	93391 2054	141773 7840	305 NA	[5] [5]	13.4	36.6	[4] [3]
May contain data from a preliminary source.											
HUMANA	7973.0 11.9	D.A. Jones, chmn. & CEO G.H. Wolf, pres. & CEO**†	3598* 807	221 -10	0 100	6941 1955	92 NA	[4] [3]	9.2	-28.5	[3] [3]
*Includes \$2.5 mil. special bonus. **Became CEO 12/1/97.											
PAYCHEX	853.0 30.4	B.T. Golisano, chmn., pres. & CEO J.T. Carlen, exec. v-p*	641 371	19 20	0 0	1678 963	431 NA	[1] [1]	29.2	9.0	[1] [1]
*Resigned 8/31/97.											
REPUBLIC INDUSTRIES	10305.6 6.5	S.R. Berrard, pres. & co-CEO H.W. Hudson, vice-chmn.	470 496	20392 73	0 0	NA 898	1373 NA	NA [1]	3.2	-32.4	NA [4]
ROBERT HALF INTERNATIONAL	1302.9 22.4	H.M. Messmer Jr., chmn. & CEO M.K. Waddell, sr. v-p	1705 820	34 23	21688 6290	46897 16869	500 NA	[4] [3]	20.0	51.6	[3] [3]
TENET HEALTHCARE	9348.5 -0.5	J.C. Barbakow, chmn. & CEO M.H. Focht, pres. & COO	2320 1552	7 11	0 0	6093 7743	235 NA	[2] [3]	4.1	-105.3	[4] [4]
UNITED HEALTHCARE	11794.5 9.5	W.W. McGuire, CEO T.H. Wills, COO	1271 515	10 9	7233 2930	22509 6498	110 NA	[5] [4]	8.9	-7.8	[4] [4]
WASTE MANAGEMENT	9188.6 -30.5	P.B. Rooney, pres. & CEO* R.S. Miller Jr., chmn. & CEO†**	2558 92	41 NA	0 13	6770 NA	112 NA	[5] NA	-2.5	-276.3	[5] NA
May contain data from a preliminary source. *Resigned 2/17/97. **Became CEO 10/29/97.											
WELLPOINT HEALTH NETWORKS	5826.4 18.6	L.D. Schaeffer, chmn. & CEO† R.A. Williams, exec. v-p†	1490 934	16 13	0 0	9334 4308	124 NA	[4] [4]	17.5	23.8	[3] [2]

31 STEEL (INDUSTRIAL: LOW TECH)

NUCOR	4184.5 16.3	J.D. Correnti, vice-chmn., pres. & CEO F.K. Iverson, chmn.	780 882	13 8	464 398	3780 4568	89 NA	[2] [4]	17.2	-19.1	[2] [3]
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32 TELECOMMUNICATIONS (TELECOMMUNICATIONS)

ALLTEL	3263.6 23.0	J.T. Ford, chmn. & CEO S.T. Ford, pres.	1365 762	2 9	3666* 178	8222 NA	151 NA	[3] NA	18.4	37.7	[3] NA
*Includes \$1.3 mil. above market earnings on deferred compensation.											
AMERITECH	15998.0 27.6	R.C. Notebaert, chmn., pres. & CEO O.G. Shaffer, exec. v-p & CFO	2642 1014	32 28	405 0	8173 2671	223 NA	[2] [1]	28.0	43.0	[2] [1]
AT&T	51319.0 19.7	R.E. Allen, chmn. & CEO* J.D. Zeglis, pres.†	3275 2078	2 47	4823 320	20623 8933	198 NA	[4] [3]	16.1	-24.9	[4] [4]
*Left office 10/31/97.											
BELL ATLANTIC	30367.9 19.2	R.W. Smith, chmn. & CEO I.G. Seidenberg, vice-chmn.†	2653 2771	26 18	4378* 3989**	11314 11256	209 NA	[2] [4]	23.5	-16.7	[3] [3]
*Includes \$4.0 mil. merger implementation bonus. **Includes \$3.0 mil. merger implementation bonus. Joined company 8/1/97.											
BELLSOUTH	20633.0 21.6	F.D. Ackerman, chmn., pres. & CEO J.A. Drummond, pres.-sub.	2136 1034	51 3	148 580	6664 4157	232 NA	[2] [2]	18.8	43.4	[2] [2]
CIENA	454.2 33.1	P.H. Nettles, pres. & CEO† L.P. Huang, sr. v-p†	422 242	29 10	0 13700	1050 14356	NA NA	NA NA	NA	NA	NA NA
FRONTIER	2352.9 5.6	J.P. Clayton, pres. & CEO R.L. Bittner, chmn. & CEO	715 508	NA -27	471* 574**	NA 3240	127 NA	NA [2]	14.2	-58.5	NA [3]
*Includes \$470,699 relocation fees. Joined company 6/9/97. **Includes \$309,344 forgiven loan amount and \$264,619 in other compensation. Passed away 8/31/97.											
GTE	23260.0 34.8	C.R. Lee, chmn. & CEO K.B. Foster, pres.	2608 1913	3 5	3247 1926	15691 10184	197 NA	[4] [4]	36.6	49.1	[2] [2]
LUCENT TECHNOLOGIES	27146.0 10.1	H.B. Schacht, chmn. & CEO R.A. McGinn, pres. & COO**†	1511* 2464*	137 23	0 10581	NA 17871	NA NA	NA NA	-14.0	NA	NA NA
*Bonus represents 9 months of data. **Became CEO 10/7/97.											
QWEST COMMUNICATIONS INTL.	696.7 3.8	J.P. Nacchio, pres. & CEO R.S. Woodruff, exec. v-p & CFO†	893 295	NA 41	7232* 9453	NA 10142	NA NA	NA NA	NA	NA	NA NA
*Includes \$7.2 mil. special bonus for joining company. Became CEO 1/4/97.											

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EXECUTIVE COMPENSATION SCOREBOARD

COMPANY	EXECUTIVE	1997 COMPENSATION			1995-97 PAY-PERFORMANCE ANALYSIS							
		TOTAL ANNUAL COMP		LONG-TERM COMP \$000	PAY VS. SHAREHOLDER RETURN			PAY VS. CORPORATE PROFIT				
		SALARY & BONUS \$000	% CHANGE FROM 1996		TOTAL COMP \$000	\$ VALUE OF \$100 INVESTED	RATING	ROE %	CHANGE IN ROE %	RATING		
SBC COMMUNICATIONS	1997 SALES \$ MILLIONS	24856.0	E.E. Whitacre Jr., chmn. & CEO	4682	28	10970	26999	200	5	25.3	-24.5	3
	ROE %	14.9	R.S. Caldwell, pres.	1700	23	3590	8646		3			3
SOUTHERN NEW ENGLAND TELECOMMS.	2022.3	D.J. Miglio, chmn., pres. & CEO	951	26	67	2388	178	1	1	40.8	77.4	1
	33.1	D.R. Shassian, sr. v-p & CFO	515	23	0	1339		1				1
SPRINT	14873.9	W.T. Esrey, chmn. & CEO	1073	-68	8688	17233	275	3	3	14.9	-45.9	5
	10.5	R.T. LeMay, pres. & COO*	613	-75	15583	22965		5				5
*Resigned 7/1/97. Rejoined company 10/31/97.												
TELLABS	1203.5	M.J. Birck, pres. & CEO	579	1	0	2898	379	1	1	25.0	14.3	1
	28.3	B.J. Jackman, pres.-sub.	409	3	4147	8200		2				2
WORLDCOM	7351.4	B.J. Ebbers, pres. & CEO	18031*	451	0	24289	311	3	3	-0.9	NM	4
	2.7	S.D. Sullivan, CFO	4000**	357	5581	11796		3				4
*Includes \$13 mil. paid under performance bonus plan. **Includes \$3.5 mil. paid under performance bonus plan.												

33 TEXTILES, APPAREL (CONSUMER PRODUCTS)

NIKE	9819.0	P.H. Knight, chmn. & CEO	2117	14	0	5624	215	2	2	23.6	11.9	2
	22.8	T.E. Clarke, pres. & COO	1498	18	1923	7938		3				3
VF	5222.2	M.J. McDonald, pres. & CEO	2265	1	433	6269	205	2	2	14.1	18.5	3
	18.5	J.P. Schamberger, v-p	1026	4	173	3307		2				2

34 TIRE & RUBBER (INDUSTRIAL: LOW TECH)

GOODYEAR TIRE & RUBBER	13155.1	S.F. Gibara, chmn., pres. & CEO	1906	21	1185	6587	202	2	2	12.7	-18.7	3
	16.5	W.J. Sharp, pres.-sub.	874	9	3729	7171		3				4

35 TOBACCO (CONSUMER PRODUCTS)

PHILIP MORRIS	56114.0	G.C. Bible, chmn. & CEO	3418	20	8938	23404	269	4	4	41.9	14.4	3
	42.3	M.H. Bring, vice-chmn.	1957	29	7934	14848		4				3
RJR NABISCO HOLDINGS	17057.0	S.F. Goldstone, chmn., pres. & CEO	4739	-30	0	12898	162	3	3	5.0	-43.2	4
	3.7	H.J. Greeniaus, pres.-sub.	1952	-1	333	9038		4				4
UST	1401.7	V.A. Gierer Jr., chmn., pres. & CEO	2575	-5	0	13147	153	4	4	137.1	-6.4	1
	100.3	R.H. Verheij, exec. v-p	1386	37	217	3467		2				1

36 UTILITIES (UTILITIES)

AES	1411.0	D.W. Bakke, pres. & CEO	1760	52	0	4681	478	1	1	16.6	-46.9	4
	13.0	T.A. Tribone, sr. v-p	1003	46	2084	4778		2				5
AMEREN	3326.5	C.W. Mueller, chmn., pres. & CEO	655	8	0	1838	148	2	2	12.7	-5.5	1
	12.8	C.L. Greenwalt, pres.-sub.††	460	-19	0	1504		2				2
BALTIMORE GAS & ELECTRIC	3307.6	C.H. Poindexter, chmn. & CEO	609	-22	425	3009	184	2	2	9.7	-15.2	3
	8.9	E.A. Crooke, pres. & COO	421	-24	299	2142		3				3
CAROLINA POWER & LIGHT	3024.1	W. Cavanaugh III, pres. & CEO	960	13	24	2574	187	2	2	13.9	15.5	1
	13.6	W.S. Orser, exec. v-p	483	7	12	1396		2				1
CINERGY	4352.8	J.E. Rogers, vice-chmn., pres. & CEO	1055	-15	2001	10180	194	5	5	13.6	80.4	3
	14.3	J.H. Randolph, chmn.	921	6	603	4844		5				3
CONSOLIDATED NATURAL GAS	5710.0	G.A. Davidson Jr., chmn. & CEO	1042	8	1051	3935	193	3	3	9.2	53.9	2
	12.9	D.M. Westfall, sr. v-p & CFO	398	9	0	1042		1				1
DOMINION RESOURCES	7436.3	T.E. Capps, chmn., pres. & CEO	1274	26	130	3901	145	4	4	8.8	-23.8	2
	7.9	N.B. Askew, exec. v-p	690	NA	456	NA		NA				NA
DTE ENERGY	3764.0	J.E. Lobbia, chmn. & CEO	874	37	61	2293	162	2	2	10.9	-0.4	2
	11.7	A.F. Earley Jr., pres. & COO	650	43	34	1666		3				3
DUKE ENERGY	16308.9	W.H. Grigg, chmn. & CEO†	1128	16	705	4271	167	4	4	13.3	-8.0	2
	12.0	R.B. Priory, chmn. & CEO*	1029	72	397	2861		4				2
*Became CEO 6/1/97												
EDISON INTERNATIONAL	9235.1	J.E. Bryson, chmn. & CEO	1711	11	0	4565	217	3	3	11.7	9.6	2
	12.1	S.E. Frank, pres. & COO-SCE	979	4	0	2814		3				2
ENERGY	9561.7	E. Lupberger, chmn. & CEO	1057	-19	0	4504	169	4	4	5.8	-31.3	2
	3.7	J.L. Maulden, vice-chmn.	513	-29	0	2472		4				2
FIRSTENERGY	2823.9	W.R. Holland, chmn. & CEO	877	20	180	2559	192	2	2	12.1	-2.7	2
	11.8	H.P. Burg, pres. & CFO	493	55	70	1267		1				1
FPL GROUP	6369.0	J.L. Broadhead, chmn., pres. & CEO	1788	15	1492	8420	191	4	4	12.7	3.2	2
	12.8	P.J. Evanson, pres.	990	12	307	3344		4				2
GPU	4143.4	F.D. Hafer, chmn., pres. & CEO*	806	45	67	1907	192	1	1	11.8	69.9	2
	10.8	I.H. Jolles, sr. v-p	436	-4	86	1573		2				2
*Became CEO 5/1/97												
HOUSTON INDUSTRIES	6873.4	D.D. Jordan, chmn. & CEO	2721	34	5044*	12761	185	5	5	9.5	-30.5	2
	8.4	R.S. Letbetter, pres. & COO	929	24	152	2700		3				2
*Includes \$897,657 one-time life insurance payment.												
NEW CENTURY ENERGIES	3342.5	W.H. Brunetti, vice-chmn., pres. & COO	545	-17	232	2092	195	1	1	12.0	11.0	1
	11.1	B.D. Helton, chmn. & CEO*†	805	NA	8	NA		NA				NA
*Became CEO 8/1/97.												
NORTHERN STATES POWER	2733.8	J.J. Howard, chmn., pres. & CEO	881	-15	477	4170	157	4	4	11.6	-21.7	1
	9.5	P.E. Anders, v-p	432*	NA	0	NA		NA				NA
*Includes \$150,000 to join company and \$50,000 in lieu of restricted stock grant. Joined company 5/1/97.												

COMPANY	EXECUTIVE		1997 COMPENSATION			1995-97 PAY-PERFORMANCE ANALYSIS							
			TOTAL ANNUAL COMP		LONG-TERM COMP. \$000	PAY VS. SHAREHOLDER RETURN			PAY VS. CORPORATE PROFIT				
			SALARY & BONUS \$000	% CHANGE FROM 1996		TOTAL COMP \$000	\$ VALUE OF \$100 INVESTED	RATING	ROE %	CHANGE IN ROE %	RATING		
	1997 SALES \$ MILLIONS	ROE %											
AMERICO	6278.0		F.W. Buckman, pres. & CEO	635	-41	470	3627	177	[3]	9.9	-59.7	[5]	
	5.0		R.T. O'Brien, sr. v-p & CFO†	288	-18	128	1496		[2]			[4]	
AMEREN	4617.9		C.A. McNeill Jr., chmn., pres. & CEO	881	22	0	2477	122	[3]	11.8	29.6	[2]	
	11.7		D.M. Smith, pres.-sub.	480	13	0	1365		[3]			[1]	
AMEREN	15399.9		S.T. Skinner, chmn. & CEO	996	47	632	3576	151	[3]	10.5	-26.8	[3]	
	8.0		R.D. Glynn Jr., chmn., pres. & CEO*	790	70	409	2306		[4]			[4]	
*Became CEO 5/31/97.													
AMEREN	6369.2		E.J. Ferland, chmn., pres. & CEO	712*	-28	109	3138	151	[3]	11.4	-15.9	[2]	
	10.8		L.R. Codey, pres. & COO-sub.	435*	-25	50	1823		[3]			[2]	
*1997 bonus has not been determined.													
AMEREN	7945.6		E. Nye, chmn. & CEO	1085	19	523	3979	156	[3]	6.6	15.4	[3]	
	9.7		J.S. Farrington, chmn.	790	-13	316	3670		[5]			[4]	
AMEREN	4409.6		K.E. Bailey, chmn., pres. & CEO	1000*	5	1121	6190	369	[2]	10.1	-9.5	[4]	
	10.1		S.L. Cropper, chmn., pres. & CEO-sub.	473	6	53	2449		[1]			[3]	
*Excludes portion of bonus paid in restricted stock													

ALPHABETICAL LIST OF COMPANIES

The number following each company name identifies the Scoreboard category under which it is listed

Laboratories 11	Black & Decker 15	Deere 15	Georgia-Pacific 24	Lockheed Martin 1	Pfizer 11	SunAmerica 21
16	Boring 1	Delta Air Lines 2	Gillette 25	Loews 21	PG&E 36	SunTrust Banks 5
21	Bristol-Myers Squibb 11	Diamond Offshore 23	Global Marine 23	Lucent Technologies 32	Pharmacia & Upjohn 11	Synovus Financial 5
21	Browning-Ferris 30	Digital Equipment 22	Golden West 21	Marsh & McLennan 21	Philip Morris 35	Sysco 13
erson (H.F.) 21	Burlington Northern Santa Fe 27	Disney (Walt) 17	Goodyear Tire & Rubber 34	Marshall & Isley 5	Phillips Petroleum 20	Tellabs 32
ducts & Chemicals 8	Burlington Resources 20	Dominion Resources 36	GPU 36	Mattel 17	Pioneer Hi-Bred 13	Tenet Healthcare 30
erson's 28	Cadence Design Systems 22	Donaldson, Lufkin & Jenrette 21	Grainger (W.W.) 30	Maxim Integrated Prods. 12	Pitney Bowes 22	Tenneco 9
18	Campbell Soup 13	Donnelley (R.R.) 30	Green Tree Financial 21	MBIA 21	PNC Bank 5	Tenaxo 20
eny Teledyne 9	Capital One Financial 21	Dover 15	GTE 32	MBNA 5	PPG Industries 7	Texas Instruments 12
Signal 9	Cardinal Health 29	Dow Chemical 8	Guidant 11	McGraw-Hill 26	Praxair 8	Texas Utilities 36
te 21	Carnival 17	Dow Jones 26	Halliburton 23	Medtronic 11	Procter & Gamble 25	Textron 9
32	Carolina Power 36	Dresser Industries 23	Harcourt General 9	Mellon Bank 5	Progressive 21	3Com 22
ada Hess 20	Caterpillar 15	DTE Energy 36	Harley-Davidson 17	Mercantile Bancorp. 5	Provident Financial 5	Time Warner 26
en 36	CBS 26	Duke Energy 36	Harris 12	Merck 11	Public Service Ent. 36	Times Mirror 26
ca Online 22	Cendant 30	Dun & Bradstreet 21	Hartford Financial Services 21	Merrill Lynch 21	Quaker Oats 13	Torchmark 21
can Express 21	Ceridian 22	DuPont 8	Hartford Life 21	MGIC Investment 21	Qwest Commun. 17	Transamerica 21
can General 21	Charter One Financial 21	Eastman Kodak 17	HBO 22	Micron Technology 12	Ralston Purina 13	Travelers Group 21
can Home 11	Chase Manhattan 5	Eaton 12	Health Management Assocs. 30	Microsoft 22	ReliaStar Financial 21	Travelers Property Casualty 21
can Intl. Group 21	Chevron 20	Edison International 36	Healthsouth 30	Minnesota Mining 19	Republic Industries 30	Tribune 26
tech 32	Chubb 21	Electronic Data Systems 22	Heinz (H.J.) 13	Mobil 20	Republic New York 5	Tricon Global Restaurants 14
n 11	Ciena 32	EMC 22	Hercules 8	Molex 12	Reynolds Metals 18	TRW 9
o 20	Cigna 21	Emerson Electric 16	Hershey Foods 13	Monsanto 8	Rite Aid 29	Tyco Intl. 15
2	Cincinnati Financial 21	Enron 30	Hewlett-Packard 22	Morgan (J.P.) 5	RJR Nabisco 35	Tyson Foods 13
!	CiNergy 36	Entergy 36	Hillmanbrand 19	Morgan Stanley, Dean Witter 21	Robert Half International 30	U.S. Bancorp 5
uth Bancorporation 5	Cintas 30	Equifax 21	Hilton Hotels 14	Morton International 8	Rockwell International 12	UAL 2
g Devices 12	Cisco Systems 22	Equitable 21	Honeywell 16	Motorola 12	Rohm & Haas 8	Union Camp 24
ser-Busch 6	Citicorp 5	Estée Lauder 25	Household Intl. 21	Nabisco Holdings 13	Rubbermaid 19	Union Carbide 8
1	Clear Channel Communs. 26	Exxon 20	Houston Industries 36	National City 5	SABRE Group Holdings 22	Union Pacific 27
nd Materials 15	Clorox 25	FDX 30	Humana 30	NationsBank 5	Safeco 21	Union Pacific Resources 20
r Daniels 13	CNA Financial 21	Fifth Third Bancorp 5	Huntington Bancshares 5	New Century Energies 36	Safeway 28	Union Planters 5
nd 20	Coastal 20	First Chicago NBD 5	IBM 22	New York Times 26	Sara Lee 13	United HealthCare 30
ates First Capital 21	Coca-Cola 6	First Data 22	IKON Office Solutions 9	Newell 19	SBC Communications 32	United Technologies 1
32	Coca-Cola Enterprises 6	First Security 5	Illinois Tool Works 19	Newmont Mining 18	Schering-Plough 11	UNUM 21
ic Richfield 20	Cognizant 30	First Tennessee Natl. 5	IMC Global 8	Nike 33	Schlumberger 23	UST 35
atic Data 22	Colgate-Palmolive 25	First Union 5	Ingersoll-Rand 15	Norfolk Southern 27	Schwab (Charles) 21	USX-Marathon 20
one 29	Columbia/HCA Healthcare 30	Firststar 5	Intel 12	Northern States 36	Scripps (E.W.) 26	VF 33
Dennison 10	Comerica 5	FirstEnergy 36	International Flavors 8	Northern Trust 5	Seagate Technology 22	Wachovia 5
Products 25	Compaq Computer 22	Fleet Financial Group 5	International Paper 24	Northwest Airlines 2	Sears, Roebuck 29	Walgreen 29
Hughes 23	Computer Associates 22	Fluor 30	ITT Industries 9	Norwest 5	Sherwin-Williams 7	Washington Mutual 11
iore G&E 36	Compuware 22	Fort James 24	Jefferson-Pilot 21	Nucor 31	Selecon 12	Washington Post 26
One 5	ConAgra 13	Fortune Brands 19	Johnson & Johnson 11	Occidental Pet 20	South New Eng. Tel. 32	Waste Management 30
of New York 5	Cons. Natural Gas 36	FPL Group 36	Johnson Controls 19	Old Republic Intl. 21	SouthTrust 5	WellPoint Health 30
menca 5	Cooper Industries 12	Franklin Resources 21	Kansas City Southern 27	Oracle 22	Sprint 32	Wells Fargo 5
oston 5	CoreStates Financial 5	Frontier 32	Kellogg 13	Owens-Illinois 10	St. Paul 21	Weyerhaeuser 24
rs Trust 5	Corning 19	Gannett 26	KeyCorp 5	PacifiCorp 36	State Street 5	Whirlpool 3
International 11	Costco 29	Gap 29	Kimberly-Clark 24	PaineWebber Group 21	Sterling Commerce 22	Williams 36
etworks 22	Cox Communications 26	Genentech 11	Knight-Ridder 26	Parametric Technology 22	Stryker 11	Winn-Dixie Stores 28
tearins 21	Crestar Financial 5	General Dynamics 1	Kroger 28	PepsiCo 36	Summit Bancorp. 5	WorldCom 32
Atlantic 32	Crown Cork & Seal 10	General Electric 9	Leggett & Platt 3	PepsiCo 6	Sun Microsystems 22	Wrigley (Wm.) Jr. 13
uth 32	CSX 27	General Mills 13	Lehman Brothers Holdings 21			
ire Hathaway 21	CVS 29	General Re 21	Lily (Eli) 11			
ods 13	Dana 4	Genuine Parts 30	Linear Technology 12			



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What to MIC

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computer industry has
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billion

Cover Story

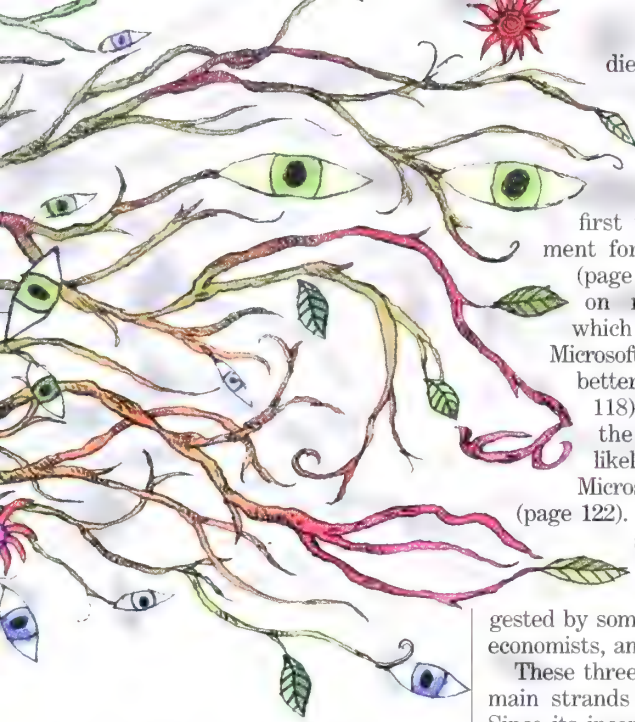
w have grown as much
soft. In 1997, Microsoft's
on in net income ac-
for 41% of the profits

of the 10 largest publicly traded
software companies, by BUSINESS
WEEK's calculation. Now, Mi-
crosoft, with its \$10 billion cash
pile and 25,700 employees, is
reaching beyond
the PC into new
markets—every-

thing from computerized toys
and TV set-top boxes to selling
cars and airline tickets over the
Internet.

The sheer pervasiveness of
Microsoft in an increasingly dig-
ital world raises profound ques-
tions: Should a single company
exercise so much economic pow-
er? And what should the gov-
ernment do, if anything?

These may well be the most
critical economic-policy decisions
facing the U.S. today. And they
are coming to a head. Later this
month, Microsoft is expected to



launch its publicity blitz for Windows 98—a new version of its operating system. This product release is a lightning rod from an antitrust viewpoint, since it integrates an Internet browser, a new product, into Windows—an existing monopoly. Any day now, the Justice Dept. is expected to head that off by trying to force Microsoft to provide an alternative version of Windows without the browser. In the face of imminent government action, Microsoft legal executives are meeting with Klein and his deputies on Apr. 10 in Washington to get a clear picture of the government's concerns and see if they can address them, insiders say.

As part of its suit, Justice could also aim at curbing a wide range of allegedly anticompetitive practices, including exclusionary contracts and Microsoft's control of the opening screen. And trustbusters are marshalling forces for a possible second suit, which could be filed during the next several months, that could focus on some of the company's stakeholds in video technology, Apple Computer Inc., and other businesses.

TOUGH QUESTIONS. For Microsoft's part, executives deny any wrongdoing and say that government interference will hurt not only their company but the entire industry. Microsoft Chairman William H. Gates III explains it this way: "The software industry's success has not been driven by government regulation, but by freedom and the basic human desire to learn, to innovate and excel."

The stakes are enormous: Any government action runs the risk of hobbling the most dynamic sector of the economy. And even though Justice's antitrust staffers have been quizzing industry executives in recent days on suitable reme-

dies, they have received no clear-cut answers.

So **BUSINESS WEEK** has assembled a package examining three alternative strategies. The first piece analyzes the argument for leaving Microsoft alone (page 115). The second focuses on regulatory solutions, in which the trustbusters restrict Microsoft's behavior to give rivals a better chance at surviving (page 118). And the third explores the possibility, however unlikely, that Justice could break Microsoft up into two companies (page 122). While Justice insiders say such a radical move is not under serious consideration, it is a remedy suggested by some computer executives and economists, and so deserves a hearing.

These three approaches represent the main strands of U.S. antitrust policy. Since its inception more than 100 years ago, that policy has swung between relying on market forces, policing conduct, or trying to make major structural changes to ensure competition.

Certainly, there's strong sentiment for leaving Microsoft alone. The supporters of a do-nothing policy believe that the software industry naturally coalesces around a single standard, so that artificially creating competition in PC operating systems and related software would be inefficient. What's more, the presumption is that market pressures and the threat of new technologies will keep Microsoft from taking advantage of its position.

But the idea of letting the market operate unchecked has not proved acceptable to the Justice Dept. Rather, it has chosen the middle ground—trying to regulate Microsoft's business practices. In 1995, it won a consent decree that prohibited certain licensing practices for Windows 95 as well as tying the sale of

one product to another. Still, focus solely on conduct remedies could be problematic: Most of these options would mean intrusive government oversight.

There is precedent for a third option: breaking up Microsoft. Worries about dominant companies exercising too much power have been part of antitrust policy from its beginning through the breakup of Standard Oil in 1911 up to the split of AT&T in the early 1980s. Now, the reach of Microsoft has brought the same sentiments back to life. "Ultimately, society can't stand that kind of concentration of power," says Robert Ingle, president of Knight-Ridder New Media, who competes against Microsoft's news and local entertainment Web sites.

DEJA VU. It's not just populism, though, that motivates regulators. Even if Microsoft has been playing by the rules, its dominant position could prove harmful to the economy. Consider innovation: Microsoft has done an excellent job of improving its product line over time, what Harvard business school professor Clayton M. Christensen calls "sustaining innovations." But many of the improvements came after rivals pointed the way—Apple Computer Inc.'s graphical user interface, for example. This is because large companies, by nature, are unlikely to encourage "disruptive" in-

novation—entirely fresh approaches that could kill off current technology.

Oddly enough, Microsoft itself in some ways was the child of antitrust. The government's 13-year attempt to break IBM, though it failed, profoundly affected Big Blue's behavior. Deals with companies such as Microsoft were done without taking an equity stake. "We didn't want to look like we were stepping on a small guy," says an IBM insider. And one can argue that the outcome was a boon: We wound up with the most vibrant high-tech industry in the world.

So what's the right thing to do? For now, on, and judge for yourself.

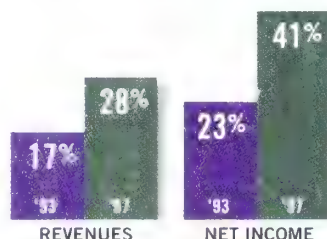
Cover Story

THE MICROSOFT MONEY MACHINE

Its Dominance Is Growing...

...Even As It Racks Up Big Profits

MICROSOFT SIZE AS A PERCENT OF 10 LARGEST PUBLICLY TRADED SOFTWARE COMPANIES



DATA: DRI/McGraw-Hill, BUSINESS WEEK

BIGGEST PROFIT MARGINS AMONG 500 COMPANIES IN S&P 500 INDEX

MBIA	57.2
MGIC INVESTMENT	37.2
SUNAMERICA	34.5
UST	31.3
MICROSOFT	29.7
INTEL	27.7
PARAMETRIC TECHNOLOGY	27.4
AMGEN	26.8
COMPUTER ASSOCIATES	24.7
MELLON BANK	23.6

UNCLE SAM LEAVES BILL GATES ALONE

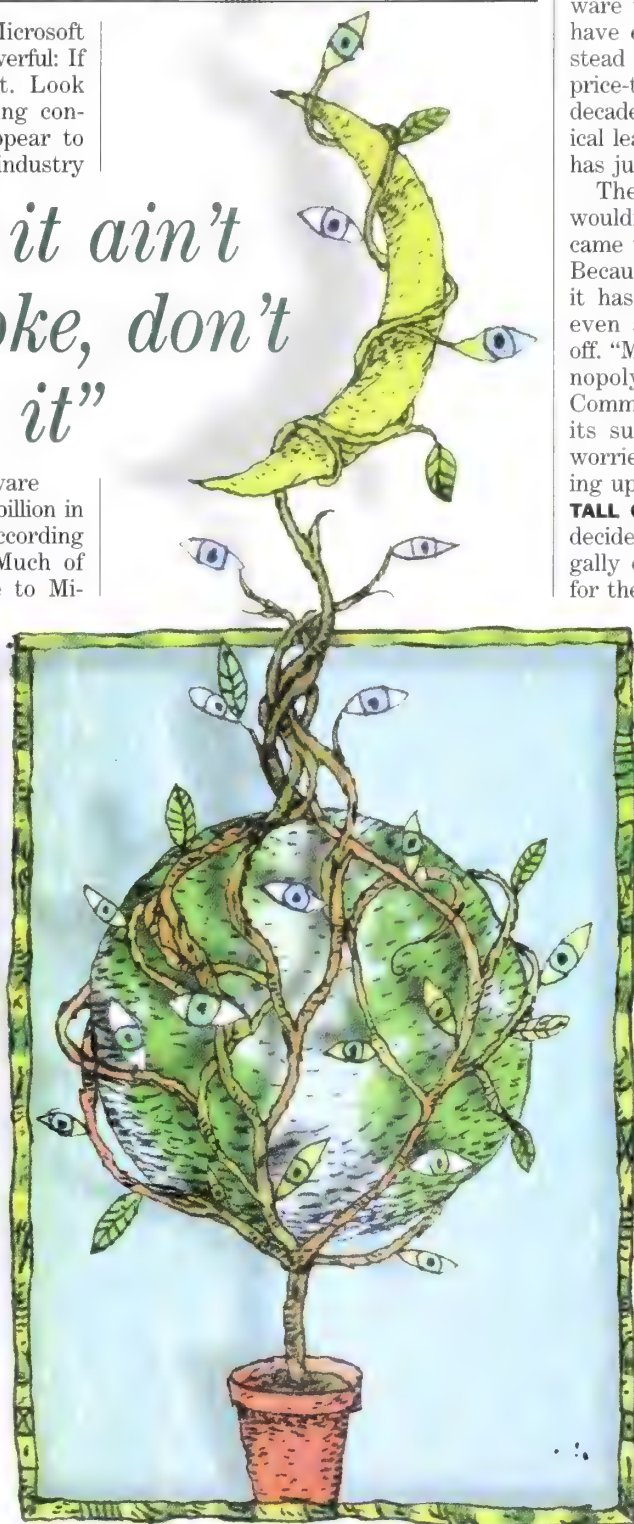
argument for leaving Microsoft alone is both simple and powerful: If it ain't broke, don't fix it. Look at the company hurting consumers? Does the economy appear to be suffering? Is the computer industry

experiencing a lack of competition or innovation? The answer is a resounding no in every count. Consider the statistics. The number of software companies compounded in the last year was twice as many

in 1990. Industrywide software sales have grown from \$39 billion in 1990 to \$122 billion last year, according to International Data Corp. Much of the good news is attributable to Microsoft. The company's Windows operating system runs on 75% of personal computers. And its more powerful sibling, Windows NT, accounted for 15% of all network servers sold last year. Those nearly 100 million programs—along with Intel Corp.'s microprocessors—help establish economies of scale for PC makers that have pushed the price of an average desktop computer down 15% in just two years, from \$2,192 in 1996 to \$1,800 today, and have fostered a thriving software-appliances industry.

STANDARD. The key to Microsoft's amazing influence is that it has become the software standard for the PC industry. As such, thousands of software makers, tens of thousands of independent software companies, and millions of individual programmers depend on it. The Windows standard assures those companies and programmers of a huge market for their goods. And, for consumers and corporate users, Windows serves as a guaranty that software will work on any of the

"If it ain't broke, don't fix it"



250 million PCs that have been shipped worldwide since 1990.

Yes, Microsoft is the chief beneficiary of its monopoly. But Microsoft got where it is today, in large part, by competing harder and smarter than its rivals. Take Apple Computer Inc., the only semblance of competition in PC operating systems. Early on, Apple made a crucial decision not to license its operating software to other PC makers—which could have established it as the standard instead of Windows—and pursued a high-price-tag strategy. Then, over the past decade, Apple squandered its technological lead and today the computer maker has just 3% of the worldwide market.

There are those who even say it wouldn't be a problem if Windows became the only operating system. Why? Because Microsoft's track record shows it has steadfastly improved Windows, even as the competition has dropped off. "Microsoft doesn't behave like a monopoly," says Mark Hoffman, CEO of Commerce One Inc., which has hitched its success to Windows. "It's always worried about another competitor coming up and beating it."

TALL ORDER. Even if the Justice Dept. decides that Microsoft has behaved illegally or is becoming just too powerful for the good of the software industry, it

must establish that consumers have been harmed. That will be a tall order—given the PC industry's track record for keeping prices low, even while adding new features.

One of the things competitors complain about most is Microsoft's practice of adopting others' innovations and integrating them into its own operating system. In the past three years, Microsoft has snapped up or taken equity stakes in more than two dozen startups with leading-edge technology. Such acquisitions bring great benefits to consumers. And by packing into Windows new technologies such as the graphical user interface, data compression, and faxing capabilities, Microsoft has spared consumers from having to buy those features separately and stitch them together. To be sure, Windows has risen in cost: In 1990, the retail upgrade cost was \$50. Now it goes for \$109. Microsoft says that's because Windows is now much more powerful. Nonetheless, higher prices are remarkable in an industry where prices are falling.

Meanwhile, there's no short-

age of innovation in Windows applications being made by other companies—including corporate software for tracking inventory and order-taking, as well as programs designed for traveling workers and games and education software.

And, although Microsoft may look invincible, some of the company's most feared initiatives have bombed. Intuit Inc. remains the No. 1 maker of personal-finance software, despite Microsoft's repeated attempts to topple the Silicon Valley company. When all else failed, Microsoft tried to acquire Intuit Inc. in 1994—but was blocked by the feds. The following year, rivals were fretting about Microsoft's launch of Microsoft Network

The next big thing could shake Microsoft

ful—shifts the balance of power. In the 1980s, it was nearly impossible to believe that IBM could be unseated from its high-tech throne. But the computer giant failed to anticipate the PC revolution and allowed Microsoft to control key standards that it rode to dominance.

Similarly, the Internet or some unforeseen phenomenon could topple Microsoft someday. That kind of technolog-

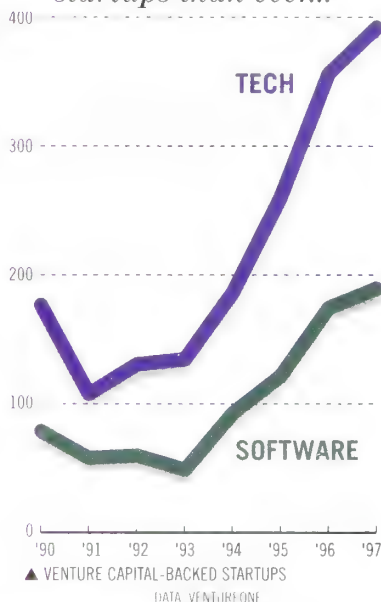
government spotlight trained on Microsoft may ensure the giant does not overstep its bounds. Bill Gates has already shown that he's willing to budge—at least a bit: A month ago, on the eve of his appearance before the Senate Judiciary Committee, Microsoft unilaterally altered contracts with Internet service providers, lifting provisions requiring them to favor Microsoft's browser over that of Netscape Communications Corp. as a condition for getting referrals from the Windows screen. "We listen to criticism," says William H. Neukom, Microsoft's chief counsel. "If there are sideshow issues that we feel we're not wrong about, we see it's in the company's and our customers' best interests to move on—we're willing to do that."

Microsoft is now reconsidering

WHY MESS WITH A GOOD THING?

There are more new startups than ever...

...And some are finding a home at Microsoft



MICROSOFT'S RECENT BUYS

12/31/97 Spends \$395 million in stock to acquire HotMail, a free Web E-mail service used by 9 million people

8/11/97 Invests \$45 million in speech-recognition software maker Lernout & Hauspie

8/6/97 Invests \$150 million in Apple as part of a technology-swapping deal

8/5/97 Acquires Vxtreme, which makes software for sending video over the Net

7/21/97 Invests \$30 million for a 10% stake in Real Networks, another maker of video streaming technology

6/26/97 Forms a joint ven-

ture with First Data for online bill paying

6/13/97 Acquires Coopers & Peters, which makes Java-based interface software

6/6/97 Invests \$1 billion in cable-TV operator Comcast

5/7/97 Acquires Dimension X, maker of Java tools for multimedia

4/6/97 Acquires WebTV for \$425 million

3/3/97 Acquires Interse, which makes Web-site analysis software

10/96 invests \$10 million for an equity stake in VDOnet, another video streaming company

DATA: BUSINESS WEEK

(MSN), an online service that would compete with America Online Inc. Microsoft planned to include the MSN icon right on the Windows opening screen, so customers could sign up for the service with a single mouse click. Three years later, there's not much clicking: MSN has gained just 2.5 million subscribers, while AOL has zoomed to more than 11 million.

Beyond these small skirmishes, there's a bigger force at work that could keep Microsoft in check: the amazing capacity of the computer industry to correct itself through innovation. Every decade or so, a seismic change in technology comes along that alters the rules of computing and—if the combatants aren't care-

ful break "will make Microsoft irrelevant in our generation," predicts venture capitalist Roger McNamee, a partner at Integral Capital Partners. Several years from now, the computing landscape could well be dominated by smart devices, new kinds of networks and embedded systems—in cars, build-

ings, interactive television, and credit cards—for which Mi-

crosoft's general-purpose operating systems are not well suited. Whether the technological successor is Sun Microsystems Inc.'s Java or a software scheme yet to be hatched in a garage, it's likely to create a new powerhouse—until the next big thing comes along.

In the meantime, simply having the

way it handles quid pro quo relationships with the content partners whose Web sites are featured on the Windows 98 opening screen inside its "Channel Guide." (Microsoft can afford to rethink this, since it admits that the channels far drive little traffic.)

Will Microsoft change its behavior when sizable profits are at stake? Probably not. That may yet prompt the government to take action. But any tinkering could damage one of America's most successful companies—and a vibrant industry along with it. Says Robert Taylor, a law partner at Howrey & Mon in Menlo Park, Calif.: "The notion that we can make a system better when it is functioning perfectly well should be viewed with skepticism."

Cover Story

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JUSTICE SLOWS THE GIANT WITH 'SURGICAL STRIKES'

In Silicon Valley, there's a catch phrase that's applied to the fool who falls for a line of reasoning that's passionately argued, seemingly logical, yet ultimately unsupportable: "He drank the Kool-Aid"—a reference to the Jonestown suicide pact. And, according to critics of Microsoft Corp., anybody who swallows the argument that the software titan is a national treasure and therefore shouldn't be messed with has done just that.

Sure, they'll agree, Microsoft's Windows helped spawn the personal-computer revolution. That has been good for the high-tech industry, the economy, and consumers. But, critics say, Microsoft has gone too far. It has unfairly squashed software competitors. And now it's using its Windows desktop monopoly to extend its dominance to key emerging markets such as the Internet and a new crop of "smart" appliances.

Some antitrust experts are crying foul. The history of computing may suggest that no one company will rule for long—but then the world has rarely dealt with the ultra-competitiveness of Gates. Consider how effectively his company has become a top player on the Net, the next crucial technology battleground. Microsoft has grabbed some 40% of the Web browser market in just three years, in part by giving its Internet Explorer away free and by pressing PC makers to ship it as a condition of licensing Windows. Because Microsoft has woven browsing into Windows 98, due in June, it is practically assured of owning that market.

GIVING IT AWAY. What's more, Microsoft is doing the same with Windows NT, bundling freebies including a basic Web server—making it difficult for smaller competitors such as Netscape Communications Corp. And the software giant has poured hundreds of millions of dollars into creating Web sites offering travel reservations, mortgages, car buying, news, and entertainment services.

All of this adds up to a Big Brother scenario: a world where computers are everywhere—and Microsoft software controls them. What's more, by owning the first screen that people see when

they turn on their computers, Microsoft is in a position to funnel Web surfers to its own sites and, potentially to charge monopoly rents to other companies for a piece of that beachfront real estate.

In the absence of any formidable competition, there won't be much pressure on the company to keep a lid on prices, either. Already, it has phased out the pricing deals that allowed corporations to pay for server software based on the number of people who are using it at any one time—rather than the number of people who are

equipped to use it. That simplified contracts, Microsoft says, but it raised the overall cost of a license as much as fivefold for some customers, say analysts.

At the same time, Microsoft is

couraging corporate customers to adopt Windows NT as the software of choice

for their desktop machines. Analysts estimate that Microsoft gets an average of \$80 or more for NT from PC makers—double what it gets for Win95. So while

Cover Story



ices are falling, Microsoft gets an larger piece of the pie.

cause of worries over such power, likely that Justice antitrust chief will choose the "do nothing" option. Considering all his saber-rattling, feel considerable pressure to take 1. "If they bring no case, they'll be viewed as wimpy," says Joe Sims, aington antitrust lawyer.

leed, Klein & Co. are now studying potential "surgical" strikes—law—that would target specific anticompetitive practices, say insiders. His would be to devise a special set of competition rules just for Microsoft. The guidelines would come from four remedies, which could be applied alone or in combination. Each one is what's alleged to be a distinct practice:

Fair Contract Remedy

guidelines would limit Microsoft's ability to deter rivals from selling rivals' gear

of the most pervasive complaints about Microsoft is that it exploits its monopoly power by coercing business partners to agree to exclusionary deals. PC makers. It forced them to ship Internet Explorer browser with each computer as a condition of their Windows licensing contract. That has been the problem. But the company still requires PC makers to show the Windows desktop icons—as mapped out by Microsoft—when a computer is turned on. That desktop must include icons for Microsoft products such as the Internet Explorer and Microsoft Network.

Microsoft also has cut deals with Internet service providers (ISPs) requiring them to promote its browser to customers who sought out the ISP based on information from the Windows desktop. Microsoft backed off, but there's a fight to prevent it from doing this again. Indeed, it has similar agreements with Web site operators that are referred as "channels" on Internet Explorer.

In addition, Justice is looking into allegations that Microsoft has violated terms of its license for Sun Microsystems Inc.'s Java language in an attempt to undermine it. Java can be used to create software programs that can run on any operating system and, if it is widely adopted, could loosen Windows' grip on the market.

crack down on Microsoft's dealing practices, the government could establish new "rules of the road" for

the company's business contracts. These guidelines would limit Microsoft's ability to discourage business partners from selling or promoting its rivals' products. They might also force the company to abide by Sun's conditions for using Java.

Proponents trumpet this as being much easier to administer than other remedies. The government simply has to set out its guidelines and then make Microsoft turn over its contracts to Justice. "This is best because it is in the business realm rather than the technical realm," says Carl Shapiro, an economist at the University of California at Berkeley and former chief economist in Justice's Antitrust Div.

There's a good chance that this remedy would limit Microsoft's ability to bully its business partners—especially ISPs. Unlike PC makers, these players aren't dependent on Microsoft to make their "product" successful. If the government restricted Microsoft's ability to demand exclusionary contracts, the ISPs might well do more to promote Netscape's browser and other competing products.

This solution, however, isn't guaranteed to work. In an attempt to help rival operating-system makers, the Justice Dept. applied the fair contracts remedy to Microsoft in its 1995 consent decree—but it was a case of too little, too late. The company had little trouble overcoming the contractual restrictions, since Windows already claimed some 80% of the market at that time. Moreover, this remedy is unlikely to help Netscape win more business from PC makers because of their dependence on Windows.

If the Justice Dept. brings no case, "they'll be viewed as wimpy"

The On-Ramp Remedy

Microsoft would have to stop giving its own services and content top spots on Windows

Microsoft's ownership of the Windows desktop makes it, in essence, the major on-ramp to the Information Highway. Last September, when the company introduced Internet Explorer 4.0, it began offering PC makers the opportunity to feature a so-called "channel bar" on the right side of the Windows desktop screen that would allow computer users to click on a spot, launch the browser, and then proceed to a number of Web sites. Today, the first set of channels features the software maker and several of Microsoft's handpicked partners, including Walt Disney, Pointcast, and Warner Bros.

No fair, competitors say. Terrell B. Jones, president of Sabre Interactive, which operates the travel-arrangement site Travelocity, says that Microsoft denied him the opportunity of a favored position on the Channel Guide for his site. Instead, the company gave the top spot to his rival, Microsoft's own travel site, Expedia.

Justice's on-ramp remedy could prevent Microsoft from giving its own services and content favored locations on Windows. The Justice Dept. would do this by giving control of what appears on the opening screen to PC makers, which account for some 90% of Windows sales. PC makers call this the "first boot" issue—referring to when a computer is turned on—and are itching to get their hands on the prime real estate. A similar approach was used to regulate the Sabre airline-reservation service, which travel agents use to receive flight information. American Airlines Inc. launched the system 20 years ago—and it used to list its own flights first. Now, the flights must be listed in random order.

If a court placed a blanket restriction on Microsoft's ability to dictate what Internet content appeared on the Windows desktop, it could dramatically open up competition on the Web. Shifting the power to decide which icons are situated on the opening screen to PC makers would diminish Microsoft's sway over them. PC makers would be able to negotiate with software and content companies—including Microsoft—and to differentiate their plain-vanilla machines. "We'd like to control our own screen," says Stan Shih, founder of Acer Group Ltd.

The result: PC makers would gain leverage, perhaps opening up a new revenue stream as they auctioned off

space to the highest bidder. Internet-content companies, meanwhile, would no longer face the prospect of begging Microsoft for a prominent spot on the Windows screen.

The à la Carte Remedy

Microsoft would have to sell its features separately, rather than include them free in a package

To prevent Microsoft from folding other features and services into its dominant operating system, Justice could try to force the company to market many of these as separate products, or à la carte. Instead of selling Windows 98 to Compaq Computer Corp. for \$45, say, Microsoft would be forced to offer the PC maker a basic operating system for \$35. A browser might cost an additional \$10. And new features that are coming down the pike, such as speech recognition, would come with their own price tags.

The goal: to force Microsoft to sell new technology for its real cost of development rather than including it free of charge in Windows. Such bundling gives PC makers and consumers little incentive to buy competing products. The à la carte remedy would wipe out that advantage, says Washington antitrust lawyer Douglas E. Rosenthal, and "would respond to charges that small companies that are making better software are not getting a chance."

To be sure, many in the software community object vehemently to this notion of "forced unbundling." They argue that integrated functions, such as browsers and speech recognition, make operating systems better and easier to use—and that these are not necessarily separate products.

And many lawyers and techies, alike, abhor the idea of government trying to define what is "operating-system" software, and what is "application" software. They fear this would inevitably lead to a situation in which a federal District Court Judge made key business decisions, much as Judge Harold H. Greene did while supervising AT&T for years. "The last thing you want is the government putting in concrete definitions of what you can do with software," says Paul A. Maritz, Microsoft's group vice-president in charge of platforms.

Theoretically, the à la carte approach would give companies such as Netscape a better shot. But in reality, few PC makers are likely to switch from the Microsoft browser or other applications. Why? For one, Microsoft's browser wins

critical praise. And Microsoft clearly has PC makers over a barrel. They need to package Windows with their PCs, and their margins are so thin that getting a good price is crucial. Under this remedy, Microsoft would still have control over the price of the basic operating system.

As a result, it's unlikely that the à la carte solution alone would prompt computer makers to risk angering Gates by choosing rival programs. This would be especially true if the price for a stripped-down Windows was the same or not that much less than the browser-loaded version.



Klein may seek special rules just for Microsoft

The Public-Access Remedy

This approach would ensure that Microsoft open its operating system to the public

A more radical solution to the problem is to force the company to make its operating system public property—to a certain extent. The code that makes up Windows, as with most software, is private property protected under copyright law. Because Microsoft controls its Windows code, software developers must rely on applications programming interfaces (APIS) that work with it. Essentially, these APIS are hooks in the operating system that allow other companies to make their products work with Windows. This situation sets up the potential for Microsoft to favor its own applications group with hard-to-get information about Windows APIS.

Not so, says Tod Neilsen, Microsoft's director of developer relations. He insists the company gives outside software companies the same information about Windows APIS as its own applications developers—and at the same time. But some software executives have long complained that Microsoft occasionally delays release of APIS. Netscape, for in-

stance, claims Microsoft withheld information about Windows NT to get an advantage over Netscape's Web server software.

Justice is looking at ways to ensure there is no favoritism. One possible solution frequently talked about among software developers: having the government supervise Microsoft's release of APIS. This would likely require installing some sort of independent auditing body on the Microsoft campus—probably under the supervision of a judge—to approve the interfaces and disburse them to software makers.

Something similar to the "Public Access" remedy was done during the 1982 breakup of AT&T, when a judge forced local phone companies to open their switching systems to competitors. Sure enough, that required a lot of bureaucratic oversight. But according to Berkeley's Shapiro, this may be "a rare case where it is justified" because application developers rely on Microsoft assurances that its operating system is open.

It's unclear, though, whether there is any skulduggery surrounding APIS. In spite of cries for the open access remedy, complaints that Microsoft withheld information about its software have always been sketchy and are becoming increasingly rare. The company, after all, has a strong incentive to give outside developers accurate information to keep up a steady flow of Windows applications. Even Sybase Inc. CEO Mitchell E. Kertzman, one of Microsoft's loudest critics, says that, "They're very timely with sharing technology. They don't withhold it."

So which of the remedies, if any, will the Justice Dept. seek? Unless scheduled talks with Microsoft result in a settlement, the feds are expected to bring an initial suit targeting Windows 98 by the end of April. The agency probably would seek an injunction incorporating a number of quick temporary remedies, including versions

the à la carte, a ramp, and fair-tract solutions.

Klein is sensit-

to the problems his surgical-strike tactic could raise. "In thinking about a remedy you don't want to set in place a procedure where you become a de facto regulatory commission monitoring all of their activities," he said in a recent interview with BUSINESS WEEK. But as frightening as this may be, many people consider the prospect of leaving Microsoft alone worse.

Cover Story

UNDERNEATH ITS COLD, WICKED EXTERIOR
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THE FEDS SPLIT MICROSOFT IN TWO

The most extreme option open to the Justice Dept. is an outright breakup of Microsoft Corp. The government has rarely tried to split up monopolies, preferring less dramatic approaches. Yet from Standard Oil in 1911 through IBM and AT&T in recent decades, the willingness to use the ultimate remedy against excessively powerful companies has been a hallmark of U.S. antitrust policy. That's a key difference between the U.S. and countries such as Japan, which has built its economy around mammoth *keiretsu*—and appears to be suffering because of it.

While he's not ruling out a breakup, antitrust chief Klein has consistently said it's not a focus right now. But he faces a big problem: Piecemeal remedies may not get at the core issue—Microsoft's control of the operating system and its ability to leverage it in new markets. "If you think the evil is the structure, then the only fix is by changing these structures," says Herbert Hovenkamp, a law professor at the University of Iowa. "Conduct fixes will always look anemic."

The most outspoken proponents of a breakup, not surprisingly, are Oracle's Lawrence J. Ellison and Gary L. Reback, an attorney with the Palo Alto (Calif.) law firm of Wilson, Sonsini, Goodrich & Rosati, which represents a number of Microsoft competitors.

CORE PROBLEM. But aside from well-known Microsoft foes, the breakup option is getting serious consideration from a growing number of antitrust experts. "There is an underlying chronic problem, which is that Microsoft has been endowed by history with control over the operating system," says F.M. Scherer, a professor of corporate policy at John F. Kennedy School of Government in Boston. "That is essentially a structural characteristic, and it isn't going to go away. You solve structural problems structurally, rather than by detailed regulation."

In the long run, the most straightforward solution to the Microsoft dilemma may be to break it

into two entities: an operating-systems company and an applications company. Paradoxically, breakup, the strongest government action, may come closest to being the free-market answer. The two new Microsofts would be allowed to compete in the market as aggressively as they wished,

without bureaucrats hovering over their every move.

The idea has its merits. It would once and for all address critics' charges that Microsoft uses its Windows monopoly—and the hefty profits it generates—to gain an unfair advantage in other markets, such as office applications or Internet content. And severing the operating-systems business

from the applications business would eliminate the potential for

Microsoft to favor its own applications developers

with early information about Windows. Moreover, a breakup would alleviate the worry that a Goliath Microsoft will inevitably stifle innovation. Big companies do innovate, but incrementally. What they aren't so good at is more radical "disruptive" innovation.

"FAST FOLLOWER." Indeed, for all of Microsoft's success, most of the big new ideas in computing—whether graphical user interfaces or Web browsers—have come from others. The software maker has deftly learned to incorporate these ideas into its products. But many of its efforts to provide more value to customers, such as its current focus on simplifying Windows PCs, have come only after rivals have proposed alternatives—such as Sun Microsystems and Oracle Corp. did with network computers.

In the absence of a healthy competitive environment, the fear is that Microsoft would not be forced to improve its products rapidly. Nor would it have the necessary vision. Microsoft "has been a tremendously successful fast follower, but almost to the point where there's no one to borrow ideas from anymore," says Paul Saffo, a director at the Institute for the Future.

Slowing innovation may not look like a problem now, given the high-tech sector's dynamism. But some wonder how long that will last if Microsoft is allowed to expand its hegemony in PC software to new areas such as the Internet, although record numbers of new software companies are being created each year, fewer

Cover Story



Oddly, the strongest action may in fact be the free-market answer

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them ever reach a critical size. Most fizzle out or are swallowed up by bigger players—including Microsoft. If small, creative companies aren't allowed to grow and remain independent, innovation will be suppressed. Says Christensen of Harvard: "The economy would be better off if disruptive innovators can play in this game."

There are already signs of this "innovation ceiling." Venture funding is up, but the number of software companies going public fell to 22 last year, nearly half 1995's number—though that was at least partly because 1996's software IPOs fared poorly. Venture capitalists steer a wide berth around startups that hope to build a business in any area Microsoft competes in. And promising startups such as Netscape, Point-Cast Inc., and Diba Inc. have seen their potential dimmed by Microsoft's long shadow.

If Microsoft is left alone, "over the next 5 to 10 years, they will stifle innovation," says Stewart A. Schuster, a partner at Brentwood Venture Capital in Menlo Park, Calif. "That's not good for the industry, consumers, or the U.S.'s lead in competitiveness."

ENVIAIBLE POSITIONS. So what would a Microsoft breakup look like? Chairman Bill Gates, who owns 22.3% of Microsoft, would have to pick which side to stay with—the operating-systems company or the applications company—and divest from the other. Gates is so linked with the company he founded 23 years ago that it's hard to imagine any part of it not being run by him. But it seems obvious where Microsoft's soul resides. Jeffrey S. Raikes, a Microsoft group vice-president, sales and marketing, didn't hesitate when asked where he would go in the case of a breakup: "With Bill." And where would Bill go? "The Windows company."

No matter which corner office Gates picked, the resulting "Baby Bills" would be in enviable positions. Indeed, each one would have its own monopoly: the operating-systems company with Windows and the applications company with Office 97—a suite of desktop applications that claims some 94% of that \$5.2 billion market.

Office and Windows are Microsoft's biggest moneymakers, generating almost \$5 billion each last year and nearly \$2 billion apiece in 1998's first quarter alone. Their operating margins, 95% and

The resulting "Baby Bills" would still be monopolies



Cover Story

85%, respectively, are among the highest in the software business. Each company would have an army of roughly 5,000 programmers. The operating-systems company could be regulated. But if not, you could bet it would soon be competing with the applications company.

The advantages of such a split: increased competition and unleashed innovation. Consider, for example, the bust-up of AT&T. Under court order, AT&T's government-regulated telephone monopoly was ended, and long-distance

LONG-TERM GAIN. Gates would feebly fight any attempt to break Microsoft. But even an unsuccessful breakup case brought against Microsoft could change the company's behavior and create more room in the market for rivals. Look at IBM. The government's attempt to slice up Big Blue in the 1970s and early 1980s rattled the giant and made it less willing to squeeze out startups such as Digital Equipment Corp.—and Microsoft. While many view this kind of government houndings as undesirable, the result was a thriving minicomputer and PC industry.

A breakup of Microsoft would have mixed results—especially in the short run. It would be unsettling for the rest of the industry because PC makers and application developers depend on a steady march of Microsoft's operating-system upgrades to add capabilities to their products and drive demand by consumers and corporate customers. Any disruption hurts business. And a Microsoft split-up could cause enough confusion to temporarily stop customers from buying—putting a drag on the entire high-tech sector.

While a Baby Bill scenario would theoretically require less government oversight than middle-phased regulations, it would still be messy, requiring heavy government intervention. "I don't see a way to break up the company without regulatory oversight," says William J. Kovacic, an antitrust professor at George Mason University School of Law. "There is no clean, attractive structural solution."

In the AT&T case, a federal judge constantly had to monitor the division and resolve intercarrier pricing conflicts. Groups of people who had worked together for decades were split, some going to AT&T and others to the Bells. In some offices, switching centers, lines had to be drawn down the middle of the floor to delineate who owned what.

A Microsoft split would be equally complicated, if not more so. The cu-

TWIN GEEKS

An extreme solution would be to sever Microsoft into two parts: an operating-systems company and an applications-and-content company. Here's what they might look like:

	WINSOFT	APPSOFT
REVENUES*	\$5.97	\$5.39
PROFITS*	2	1.4
EMPLOYEES	10,000	15,000
MAJOR PRODUCTS**	Windows 98, Windows NT, Windows CE, Visual Basic, C++	Microsoft Office; Encarta; Web sites, including Expedia, Sidewalk, and MSN
HEADQUARTERS	Building #8 in Redmond	RedWest in Redmond
CEO	Bill Gates, chairman and CEO	Pete Higgins, group VP, Interactive Media Group

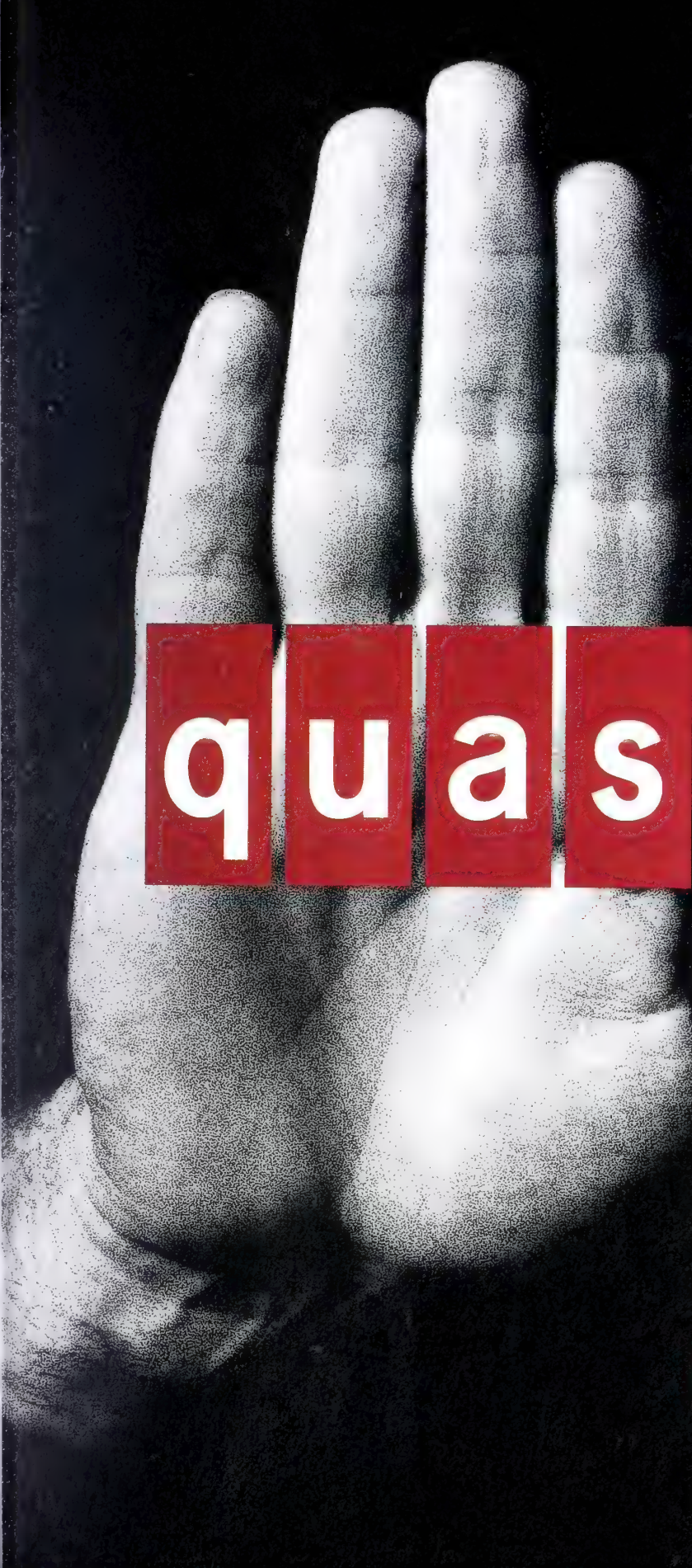
*For fiscal year ended June '97, in billions

**Up for grabs: Internet Explorer, NetShow, Back Office

DATA BUSINESS WEEK

service was opened to competition. The old monopoly company was split into the new AT&T, a long-distance carrier, and seven regional Baby Bell operating companies.

The effects were profound. Because of competition, prices plunged, quality improved, and innovation was spurred. Telephones proliferated in every corner and shape imaginable. Today, the Baby



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pany's 17,700 U.S. employees are concentrated in two locations in suburban Redmond, Wash.—a main campus with 30 buildings, and another, "RedWest," down the road, with just five. Some 8,000 additional sales, marketing, and development employees are scattered across offices in 60 countries.

It's easy to see how the operating-systems people and the applications people could be divided—they're already organized into two separate divisions. But where would browser technology go—with the operating system or the applications? Like some of the

middle-path remedies, this would put the government in the position of defining what makes up an operating system. And there's lots of arcane technology—such as a piece of basic building-block software known as

Active X—that pervades most of the company's products. There's no doubt

that a split would mean a "very messy, inefficient destruction of productive resources," says Lloyd Constantine, a New York antitrust attorney. "They would have to cut some real important hoses and valves and connections."

Breaking up Microsoft would be a

high-risk undertaking. "Structural remedies are big, they are blunt, they potentially have major consequences—the good and the bad," says Larry White, a New York University economist. A breakup would cause damage in the short run. But would it be worth while if it results in increased innovation and competition in the long run? That's the question.

By Amy Cortese and Mike Franz in New York, Susan Garland in Washington, D.C., Steve Hamm in San Mateo, Calif., and Michael Mandel in New York

Cover Story

EPILOGUE

WEIGHING THE RISKS AND REWARDS

Now comes the hard part. The Justice Dept. must ultimately decide what antitrust policy will best promote competition and innovation in the software industry. There is no obvious answer. Each of the three alternatives—do nothing, regulate, or break up—carries its own risks and rewards.

The laissez-faire solution is certainly the least disruptive in the short run and carries extra appeal given the current strength of America's high-tech sector. But it does run the risk that Microsoft will eventually squeeze out serious competition, leading to a stagnant software industry. **THIN LINE.** By contrast, the regulatory approach would have the effect of increasing competition. It would also create a bit more room for innovators, though Microsoft would still have a dominant position. The downside: Extensive government interference could paralyze the industry. Indeed, increasingly the government will find itself having to tread a thin line between stopping bad practices and designing the company's products.

Breaking up Microsoft would be a big gamble. The reward: Such a radical step could ensure years of growth

in high tech by opening the door for the next generation of innovators. The risk is that no one really understands the ingredients that make the U.S. soft-

ware industry so successful. So by splitting up Microsoft, it's possible the government could kill the goose that lays the golden eggs.

What is Justice likely to do? Right now, its main concern is Microsoft's monopoly in operating systems. That's illegal in itself, but trustbusters want to make sure that Microsoft is not maintaining its dominant position through anticompetitive practices. At the same time, regulators want to prevent a company from leveraging its strength in operating systems to create new monopolies in related markets.

That's why Justice may file suit against Microsoft by early May, seeking a preliminary injunction that would force the giant to offer a browserless version of Windows 98. The injunction might also end so-called exclusionary contracts and give PC makers control over icons on the Windows opening screen.

TEST OF LAW. Going forward, Justice officials are investigating other possibly anticompetitive practices and may bring a broader case in several months. The potential suit could add to a laundry list of alleged wrongs that concerns that Microsoft is abusing its dominant position in operating systems to give an unfair advantage to Microsoft applications and Windows—the company's broad investments in Web video streaming and its \$125 million equity stake in rival Apple Computer Inc.

Just a decade ago, the conventional wisdom was that antitrust law was irrelevant. Now, Klein is trying to make the agency meaningful in the age of the Internet. This is the test that will test whether antitrust still matters. No other is confronting trustbusters is as crucial—or as difficult.

WHAT DO YOU THINK?

DEAR READERS: Should the Justice Dept. leave Microsoft alone, bust it up, or pursue one of several regulatory paths?

Mark your responses on the form below and fax it to us at 212 512-6458. You can also E-mail your choice to hwantitrust@businessweek.com. Or you can fill out an electronic version of the survey at our Web site, www.businessweek.com. The poll will conclude Apr. 20.

To address Microsoft's dominant position in the computer-software industry, the Justice Dept. should:

☐ **DO NOTHING**

REGULATE (CHOOSE ONE OR MORE):

☐ **FAIR CONTRACT** Limit Microsoft's ability to prevent business partners from selling or promoting rivals' products.

☐ **ON-RAMP** Bar Microsoft from giving its products and services favored locations within Windows.

☐ **A LA CARTE** Force Microsoft to market its operating system, its browser, and related products separately.

☐ **PUBLIC ACCESS** Make sure that Microsoft's operating system will work with any independent software.

☐ **BREAK MICROSOFT UP INTO TWO SEPARATE COMPANIES**



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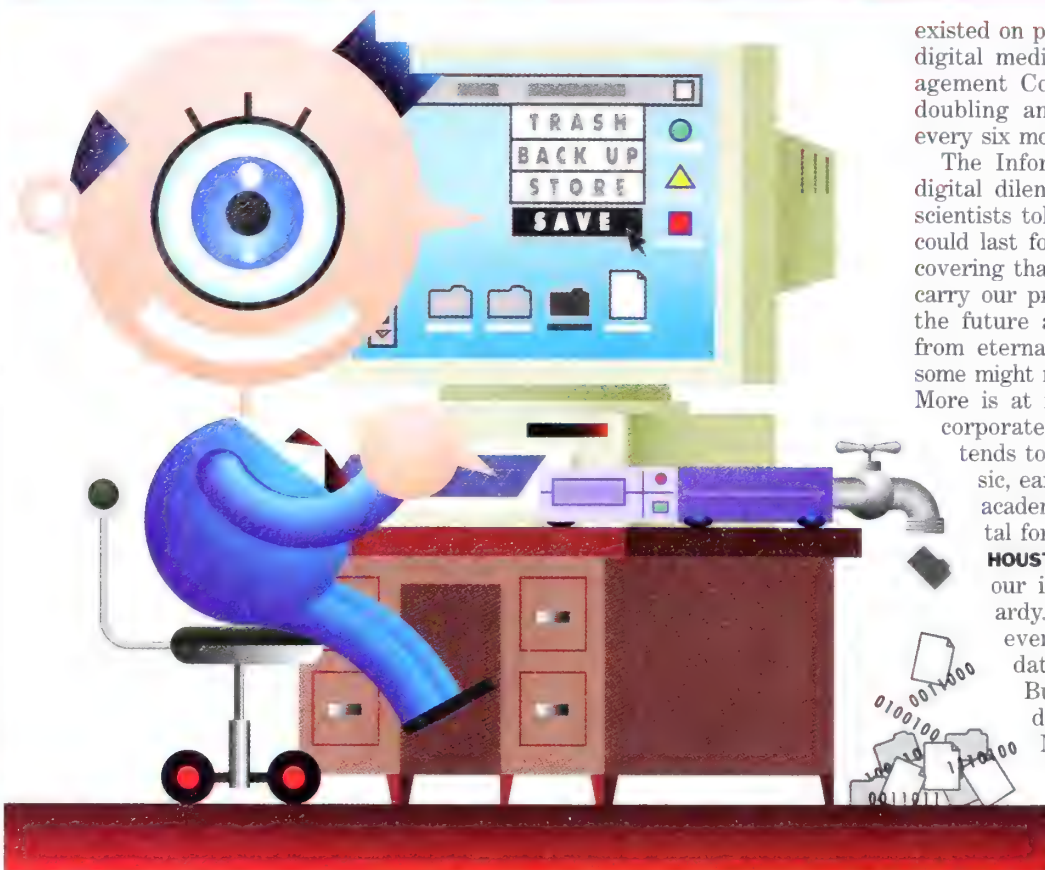
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COMPUTERS

FROM DIGITS TO DUST

Surprise—computerized data can decay before you know it

Up to 20% of the information carefully collected on Jet Propulsion Laboratory computers during NASA's 1976 Viking mission to Mars has been lost. Some POW and MIA records and casualty counts from the Vietnam War, stored on Defense Dept. computers, can no longer be read. And at Pennsylvania State University, all but 14 of some 3,000 computer files containing student records and school history are no longer accessible because of missing or outmoded software.

What's going on? The world is in a headlong rush to go digital. From Tokyo to Tampa, schools, libraries, factories, and churches are forking over great sums to computerize everything from

Johnny's latest math scores to Aunt Hattie's dental records. Computers are supposed to help us manage this information explosion by storing oceans of data that, at some later date, can be recalled at the click of a mouse.

Trouble is, all these bits of information are piling up so fast that hardly anybody is thinking about saving them. By 2000, Forrester Research Inc. estimates, one of every three Americans will be online. What's more, half to three-quarters of the data produced each day will be "born digital"—that is, it will never have

existed on paper. Says Eric Almasey, digital media expert at Mercer Management Consulting: "We're not just doubling amounts of electronic data every six months, we're quadrupling."

The Information Age is creating a digital dilemma. For years, computer scientists told us that digital 1s and 0s could last forever. But now, we're discovering that the media we're using to carry our precious information on in the future are turning out to be anything but eternal—so fragile, in fact, that some might not last through the decade. More is at risk than government and corporate records. The danger

tends to cultural legacies: new music, early drafts of literature, and academic works originate in digital form—without hard copies.

HOUSTON CALLING. To be sure, our information is not in jeopardy. There are some solutions, even new software to backup data on special paper disks. But there's no quick fix for data lost from the Viking Mars mission, for example, which was trapped on decaying digital magnetic tape, forcing NASA to call on mission specialists out of retirement to help the

agency reconstruct key data. "Digital information lasts forever, or five years—whichever comes first," says J. Rothenberg, senior computer scientist at RAND Corp.

Forget forever. Under less-than-optimal storage conditions, digital tapes and disks, including CD-ROMs and optical drives, might deteriorate about as fast as newspaper—in 5 to 10 years. Told by the National Media Lab, a St. Paul (Minn.)-based government and industry consortium, show that tapes may preserve data for a decade, depending on storage conditions. Disks—whether CD-ROMs used for games or the type used by some companies to store mission plans—may become unreadable in five years.

For consumers, the biggest worry is CD-ROMs. Unlike paper records, CD-ROMs often don't show decay until it's too late. Experts are just beginning to realize

that stray magnetic fields, oxidation, humidity, and material decay can quickly erase the information stored on them. Says Robert S. Scalet, founder of New York-based Voyager Co., which makes commercial CD-ROM books and games,

DISKS AT RISK

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"CDs have a tendency to degrade much faster than anybody, at least in the companies that make them, is willing to predict." Stein doesn't expect the CD-ROMs Voyager sells to last more than 5 or 10 years, and neither, he says, should customers.

There's another problem: the unrelenting pace of technology. Chances are good that the software needed to get at much of today's data might not be readily available in 10 years. Anyone who has tried wrestling information from a 5¼-inch floppy disk knows that. Just ask scientists conducting rain forest research. Satellite photos of the Amazon Basin taken in the 1970s—data critical to establishing deforestation trends—are trapped on indecipherable magnetic tapes no longer on the market.

But even keeping a step ahead of data decay and software obsolescence is no guarantee of escaping the problem. Companies spending heavily on sophisticated new computers and software to beat the technology reaper say they're beginning to run into a whole new problem. All too often, when they transfer information from one aging media or computer system to a newer one, not all bits make the migration. Sometimes, just a footnote or spreadsheet is lost. Other times, whole categories of data evaporate. Says Rothenberg: "It's like playing the child's game of Telephone. It doesn't take many translations from one media to another before you have lost significant aspects of the original data."

The Food & Drug Administration reports that some pharmaceutical companies are discovering errors as they copy drug-testing data that back up claims of long-term product safety and effectiveness. In several recent cases involving data transfers from Unix computers to systems running Microsoft's Windows NT operating system, blood-pressure numbers were randomly off by up to eight digits from those in original records, FDA and

company data specialists report.

Sophisticated software can catch most of the errors, but "not all the time," says Rone Lewis, vice-president of business development of Surety Technologies, a data recovery and migration firm. Some companies fear the problem could expose them to lawsuits. "In our litigation-prone age, it's harder to defend yourself if you're losing parts of your records when you migrate them," says Henry Perritt, dean of Chicago Kent College of Law.

What to do? Some government agencies have a solution—of sorts. The National Archives requires technical documentation about how the records being submitted were created. And federal regulators, including the Securities & Exchange Commission, won't take digital filings from companies they oversee unless they are sent in plain-vanilla computer formats. "Otherwise, you start getting file formats that nobody is going to be able to read in 20 years," says Bill Combs, the SEC's computer expert.

Some technology managers are urging companies to make preservation more of a priority when buying new computer systems. Ellen Knapp, chief

knowledge officer with Coopers & brand, says companies need to give in tech managers more input so that compatible systems don't compound migration problem. "Some companies have shorter visions when purchasing new technology," she says, "and end up having more compatibility problems migrating data as a result."

Ray Paddock, a director for Storage Technology Corp., says the problem is so bad for some of his clients that they're creating new databases just to decipher the data they have on tapes and disks. Others, he says, are simply keeping the old version of the software used to create documents.

NO STANDARDS. Meanwhile, the government is looking into establishing durability standards for digital media. A task force—including representatives of Eastman Kodak, IBM, and archivists at leading museums and universities—has agreed on a digital longevity test ultimately aimed at increasing the life span of CD-ROMs and other types of digital media. The only problem: So far, no manufacturer has tested its products using the age-test created by the task force. And the group is still working on a standard for magnetic tape.

Others are at work on new technologies to solve the problem. NeXT SAM Technologies in San Alamos, N.M., for example, is promoting an HD-Rosetta project, which permanently stores historical documents—but only if they are converted from digital back to analog recording formats.

But at least one remedy being offered by researchers sounds a lot more like the distant past than the future: Cobblestone Software Inc. in Lexington, Mass., is promoting SuperDisk, which uses a paper to print out complex patterns of dots and dashes representing digitized files. Cobblestone President Tom Antognini claims it should last for centuries—or about as long as old-fashioned, high-quality paper.

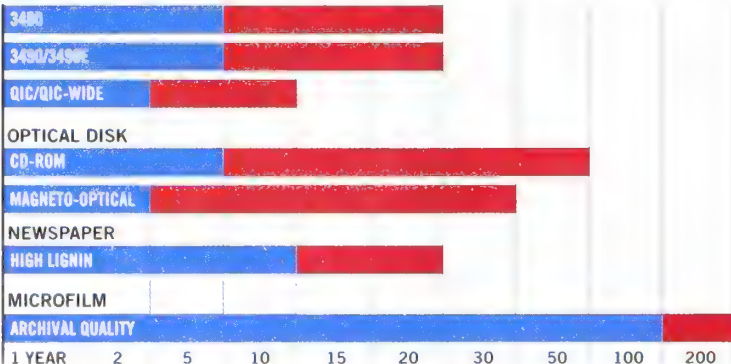
By Marcia Stepanik
in New York

DIGITAL MEDIA AGES RAPIDLY...

LENGTH OF STORAGE BASED ON PRODUCTS AVAILABLE IN 1995

■ All major products are acceptable for reliable data storage for this length of time ■ Only the best products are acceptable for storage for this length of time

MAGNETIC TAPE FORMATS



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...AND THAT'S JUST ONE PROBLEM

LONGEVITY Magnetic tape breaks down from exposure to air, heat, and humidity; optical disks can decay and surface dyes can fade in sunlight, sometimes causing the loss of information stored on them.

OBsolescence As UNIVAC drives or programs such as Word-

Perfect 4.0 become obsolete, information stored when using them may be lost, too.

MIGRATION Information can be lost or corrupted as it is transferred periodically from one type of media or computer system to a newer one.



Missa Martinez

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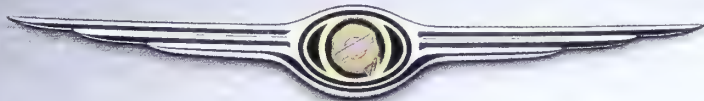
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NUCLEAR WASTE

BETWEEN A ROCK AND A HOT PLACE

Why the U.S. is snagged on the problem of spent fuel

In September, the Energy Dept. will issue a major report on the viability of Nevada's barren Yucca Mountain as a repository for America's hottest nuclear waste. A summation of years of technical studies, the report will describe how such a repository could be constructed and how much it would cost.

Lawmakers who back the Yucca Mountain scheme will use the report to quiet the project's critics, and they will redouble legislative efforts to build a temporary storage facility nearby. As the debate heats up, both sides will unleash torrents of scientific data about the supposed risks and benefits.

But the disturbing reality is that science cannot provide all the answers. Backers of the project say it will be safer and less costly than the current situation, in which more than a hundred U.S. commercial power plants and research reactors manage their own waste. Failure to build a repository will cost the government billions, says the Nuclear Energy Institute in Washington. But will Yucca Mountain be completely safe from earthquakes, water damage, or a well-planned terrorist attack? Scientists can't make any guarantees.

Some of the materials to be buried at Yucca Mountain will remain highly radioactive not for hundreds of years but for tens of thousands. How can a message be sent to warn away potential intruders 10,000 years from now, in the year 11998? No human-made edifice has lasted that long, nor has any written language.

CONTRACT-BOUND. The National Academy of Sciences took up these issues in a 1995 study. "They declared the intrusion issue 'intractable,'" says Jared L. Cohon, president of Carnegie Mellon University and chairman of an independent body called the Nuclear Waste Technical Review Board. "In other

words, there is no scientific basis for determining risks."

Debate over a central waste repository goes back to the dawn of the nuclear power industry. In the 1950s, engineers considered burning some of the waste as fuel in other reactors—an approach called reprocessing that was later adopt-

site. From day one, the decision was controversial. Washington cited Yucca's remoteness, stable geology, dry climate, and the fact that it abutted a large tract of desert that was already contaminated from nuclear bomb testing in the 1950s. But Nevada cried foul—and many environmentalists today are sympathetic. "The decision had extraordinarily little to do with Yucca Mountain's suitability as a waste site," says Daniel F. Becker, director of the Sierra Club's global warming and energy program in Washington. "It had everything to do with the weakness of Nevada's congressional delegation when this happened."

LAWSUITS. Utilities that operate nuclear reactors, and the states in which they are concentrated, have a different perspective. For better or worse, they put out, the U.S. now gets 23% of its electricity from nuclear power. The cool-



INTRACTABLE: After spending \$3 billion on studies, the government can't say whether the Yucca site is suitable

ed by France and Japan, among others. But the U.S. government rejected this solution, which yields plutonium that's usable for weapons and vulnerable to theft. Instead, it opted for permanent burial. In 1982, the government signed a contract with the electric power industry agreeing to receive nuclear waste shipments from power plants, beginning in January, 1998. And it imposed a surcharge on ratepayers to recover the costs of building the repository.

In 1987, after five years of debate, Congress selected Yucca Mountain as a

pools where spent fuel rods are stored. The site are rapidly reaching their capacity. By the end of this year, 27 sites will run out of space and will begin transferring waste to dry casks on concrete pads which erode over time. Few consider this a safe long-term solution. The industry insists that Yucca Mountain has been adequately studied. "We probably know more about this site than any place on earth," says Theodore J. Garrish, vice president in charge of nuclear waste regulation at the Nuclear Energy Institute.

The advocates' most compelling argument, however, is the legal one. In November, in response to a series of lawsuits by utilities against the U.S. Court of Appeals for the District of Columbia ordered the department to honor its obligation to take

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July 29	New York City #3
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spent fuel. The deadline to begin—Jan. 31, 1998—has passed. That riles Senator Frank H. Murkowski (R-Alaska), chairman of the Senate Committee on Energy and Natural Resources. "Electricity ratepayers have committed nearly \$14 billion [in surcharges] into the Nuclear Waste Fund," he points out. And the government has already spent \$3 billion on Yucca site studies. "The federal government has a responsibility to take this waste," Murkowski says.

Murkowski isn't alone in his insistence. Legislation to quickly establish a temporary storage facility near Yucca Mountain has been moving through Congress with bipartisan support. It may be taken up again when Congress resumes in late April. Leading the fight against the bill is Senator Richard Bryan (D-Nevada). "Any temporary facility will become, de facto, the permanent dump," he argues. The DOE takes a similar line. "How can we establish an interim site out here when we don't know whether Yucca Mountain is suitable?" asks Allen Benson, director of Institutional Affairs for the Yucca Mountain Project at DOE. President Clinton has indicated he will veto any bill establishing a temporary site in Nevada.

Gridlock is the unattractive upshot. But Senator Bryan insists that the original 1982 contract leaves the government a graceful way out of the mess. "If the DOE has no place to put the waste, then it must delay the date" for shipments to begin, he says. All sides agree that the Yucca facility will not be ready until 2010, at the earliest.

The cooling ponds where utilities store spent fuel are rapidly reaching their capacity

Meanwhile, confusing revelations are bound to continue. The September viability study may temporarily seize the spotlight. But it is just a first step in a long process. It will be followed by a draft of an environmental impact statement in 1999 and a site recommendation report in 2001. Not until then will the Nuclear Regulatory Commission decide whether Yucca Mountain can ever meet health and safety standards.

Other studies are providing ammunition for Yucca Mountain's critics. Government geologists have issued repeated assurances that the Yucca Mountain is stable, but a March 27 study published in *Science* says current hazard analyses may vastly underestimate probability of seismic activity. That's no surprise to residents. "Everyone knows there are tremors," says John A. Treichel, executive director of Nevada Nuclear Waste Task Force. The assumptions about the benefits of deep geological disposal also seem to be for grabs. The National Academy of Sciences says it will take another close look at the issues and challenges in an international workshop next spring.

Even Senator Murkowski, an outspoken Yucca advocate, admits doubt about geological disposal. But he insists that scientists are the only ones equipped to make such calls. "These issues must be addressed by people who have spent their professional lives studying what is the best thing to do," he says. "If we can't rely on them, who can we rely on?" Unfortunately, when it comes to Yucca Mountain, scientists do not have the answers.

By Neil Gross in New York

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WITH THEIR INSATIABLE hunger for realistic images, PC gamemakers have long driven technology innovation in computer graphics. The same could happen with Internet-based voice applica-



FIRETEAM: Watch your partner's back

tions. This month, Multitude Inc. of San Mateo, Calif., will launch a large-scale beta test of a game called *FireTeam*, a multiplayer combat game that lets up to four members on a team talk to each other while blasting their enemies.

First, Multitude had to deal with endemic delays over the Net, known as latency. To solve this, it developed a new way to coordinate the voices with the game. But the bigger hurdle—like so much in cyberspace—was sociological. For years, game players have been blasting each other to smithereens in silence. Multitude developers had to give them a compelling reason to speak. They set *FireTeam* up so that players can see enemies in front of them but not behind. So teammates are dependent on one another to bark commands like, "Watch your back."

□

SMALL BIOTECH COMPANY, BIG AIDS DRUG

ANALYSTS HARBOR HIGH expectations for Agouron Pharmaceuticals Inc. when it reports its third-quarter results in mid-April. Analysts are looking for revenues of \$128 million—up 231%—and a \$13 million profit, compared with a \$5 million loss a year earlier. What they're seeing is the stunning success of the 13-year-old La Jolla (Calif.) company's first product, an anti-AIDS drug called Viracept. Viracept, a protease inhibitor used in the triple-drug therapy that has helped many AIDS patients, has become the biggest new drug launch from a biotech company—sales were close to \$300 million in the first year. In fact, Viracept is the fourth-biggest new drug launch ever.

Agouron pulled this off despite grueling competition from the much larger

pharmaceutical companies Merck, Abbott Laboratories, and Hoffmann-LaRoche. Viracept has garnered a 30% market share, compared with about 35% from Merck's Crixivan. Because it's priced slightly higher, Viracept is now the best-selling protease inhibitor. It also beat the competition because it is more convenient to take and just as effective.

Still, Wall Street has not been kind to Agouron. In December, its stock plunged 25% when the company announced that Roche had pulled out of a partnership to co-develop anticancer treatments. It's not the first time Agouron has been dropped by a partner. In the early 1990s, Eli Lilly & Co. walked away from a partnership—to develop Viracept. *Larry Armstrong*

'SURROUND SOUND' IN A HEARING AID

PCS OFFER IT. SO DO VIDEO GAMES. AND NOW THE 28 million Americans who suffer from hearing loss could have it in their hearing aids. It's called 3-D sound, and thanks to a cooperative effort between Starkey Laboratories Inc., a Minneapolis hearing-aid maker, and audio equipment maker QSound Labs Inc., the technology has been shrunk onto a tiny microchip. The chip operates on just one volt of power and fits into a nickel-size hearing-aid case, which sits inside the ear canal. The device was introduced at the American Academy of Audiology's meeting in Los Angeles on Apr. 3.

3-D sound devices trick the brain into thinking it is surrounded by a symphony or it is hearing a plane buzz across the sky. They work by manipulating digital impulses to simulate the differences in the time it takes for sound waves to reach the ear closest to the sound's source and the ear that's farther away. That's the same time lag that the brain relies on to determine the origin of sound. Traditional hearing aids, which simply crank up the volume, actually impede the brain's effort to determine direction. The Starkey device recalibrates the waves, using the same mathematical formulas found in high-end audio systems. Starkey says its trials have shown a 20% improvement in hearing with the new aids, compared with conventional ones. It plans to sell the aids in September for about \$2,400. *De'Ann Weimer*

HOW TO MASS-PRODUCE 'KNOCKOUT' MICE

INTERESTED IN KNOWING the biological functions of the tens of thousands of genes that are now being discovered? Currently, one of the best methods is to breed mice in which a gene has been disabled, then see what function is affected. Trouble is, fashioning such "knockout" mice has been a time-consuming task. Scientists must target a known gene, build a probe to disable it in an embryo cell, and then grow the embryo into a mouse.

Scientists at Lexicon Genetics in The Woodlands, Tex., say they have hit on a better procedure. In the Apr.

9 issue of *Nature*, they describe a technique for mass-producing knockout mice by treating thousands of embryonic stem cells with a virus-based "vector."

In a largely random fashion, the vector disrupts one and only one—gene in each cell. Then, researchers utilize other probes to figure out which gene has been disabled. The result is a library comprising thousands of cells, each with a single gene knocked out. "Unlike the old gene targeting method, you need no prior knowledge of the gene to mutate it," explains Lexicon's research

chief Brian P. Zambrow. The procedure should be a boon to drug companies looking for promising drug targets among thousands of newly found genes. *John C.*



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It's as if Troutt is still hearing echoes

from his father, an alcoholic bartender and oil-rig worker, who told the young Kenny he would never amount to anything. When his parents divorced and Troutt's mother was forced to move her three sons into a city housing project, Troutt was determined to prove his dad wrong. A natural-born salesman since childhood, he got his start charging friends 50¢ to enter bike races that he organized. The prize: his own hand-made trophies. And a cousin, Jowanna R. Pollock, remembers him as a teen bribing her to iron one of his shirts. His payment? The offer of his autograph "someday when I'm famous."

ROCK STAR. Troutt's mother, a school cook and waitress, stressed education. "My mom was born poor, raised poor, and was going to die poor," says Troutt, with a slight Southern twang. Troutt often talks of "Mama Nadine"—now in a Florida retirement home—at Excel's boisterous sales rallies, where reps mob Troutt as if he were a rock star.

Early on, though, Troutt didn't always listen to his mama. He entered Eastern Illinois University in 1966 on a football scholarship. But by mid-year he had flunked out. Mama Nadine set the young Kenny straight. "She took me to the mirror and made me say: 'Mirror, mirror on the wall, who's the cause of all my problems?'" Troutt recalls. Back in college—this time Southern Illinois University—he squeaked by with a C- average. Troutt makes no apologies. "I have this philosophy that A and B students work for C students," he jokes.

Indeed, Troutt was already making his mark as a budding salesman. His Aunt Shirley, a saleswoman, often shared her motivational books and tapes with him, recalls his cousin Jowanna. "They would sit late at night and talk about averages, commissions and percentages," she recalls. In his senior year, he was a top producer for State Life of Indiana, \$75,000

He jokes that he sometimes wakes up in his grand mansion thinking he should check out before he is charged for another night's stay

through part-time insurance sales. College pals recall him waking early after late-night parties to head out on sales calls. "Kenny had that magnetic personality," says his college roommate and early Excel investor, Pete Wittmann.

Working for a big insurance company soon wore thin. So Troutt began selling home waterproofing. The job brought him to Omaha in 1971, where he started his own construction business. The company did well, but Troutt threw nearly all its profits into his a longtime passion for horse racing: He built a horse training facility, complete with a then-rare indoor swimming pool for the horses. With little demand in Omaha for such an extravagance, the horse ranch sucked Troutt dry. Even worse, soaring interest rates killed his construction business in 1982, and Troutt left his company—and his first wife—behind.

KENNY A. TROUTT

BORN

Jan. 8, 1948, Mt. Vernon, Ill.

EDUCATION

1970 BA, Southern Illinois Univ.

CAREER

1971-82 Started construction business in Omaha, Neb.; began breeding race horses

1982-87 Sold oil and gas leases, drilling ventures

1988-PRESENT Chairman and CEO of Excel Communications, a long-distance telecom company

FAMILY

Divorced. Second marriage in 1993 to Lisa Copeland. Two sons, 2- and 4-years old

INTERESTS

Boston Celtics fan; TV biographies. Works out with a personal trainer in home gym.

PHILOSOPHY

"\$100 to \$500 a month extra totally changes a family."

He set out for the Texas oil patch. With just \$148 to his name, he says, Troutt got work baling hay when his ramshackle pick-up truck broke down along the way. Once in Texas, he put his charm to work selling oil leases over the phone and, then, raising money for drilling deals. At first, the strikes came fast and furious. But then came dry holes and plunging oil prices. So Troutt got out, though he cleared \$200,000 in profit.

Once again, Troutt cast about for his next score. With deregulation in the wind, he decided to roll the dice on the then-fledgling world of long-distance reselling. For startup capital, Troutt turned to his oil patch investors. William A. Casner, who says he lost \$80,000 in Troutt's drilling ventures, was eager to jump in. "We were investing totally

in the individual," says Casner, who holds about 7% of Excel's shares. "Win or lose, you know Kenny is going to give everything he has."

Always a schemer, Troutt made most of his scant resources. By selling phone service on other companies' networks, he saved hundreds of millions in construction costs. And, using independent reps who sold to friends and family, he cut ad and staffing costs. In theory, the idea made perfect sense. There's no inventory for reps to carry, and they earn continuing commissions without having to refer to the customer again and again to make a sale.

But in practice, Troutt struggled to create the right marketing plan and develop billing and customer-service systems. Then, five years ago, Troutt used commissions dramatically while Excel's growing clout won it lower rates from long-distance wholesalers. Helping propel Excel was Troutt's evangelical zeal in signing up reps. Touring the country to stage glitzy rallies, he played the part of a celebrity, signing autographs for swarms of fans.

In 1993, Troutt married Lisa Copeland, then a 29 year-old sales rep for an apparel company. The couple make a powerful marketing team. Casner often speaks at "Excelebrations," annual pep rallies the company holds in Dallas, and she entertains Excel reps in the couple's mansion. But Troutt remains the star with his near-cult status among the 400,000 reps Excel claims to have signed up—though only 170,000 have been with the company for more than a year. Excel executives dismiss those who criticize its sales tactics. "Excel has shown that there's real credibility in network marketing. It's a legitimate form of selling," says Excel President John J. McLaine.

With the earlier service snafus fixed, Troutt has big plans. A merger last year with Telco Communications Group's discount long-distance operation, gave Troutt his own network for the first time. That will give him a shot at the lucrative business market. Will that give him the respect he feels he deserves? Maybe. But, for now, Troutt wants to hold on to his natural fear of the future.

By Wendy Zellner in Dallas

the new PRESENTATION TECHNOLOGY

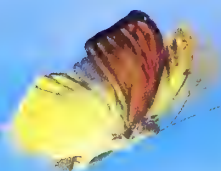


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In the Presentation Stone Age,

critical business information was often conveyed by such high-tech visual aids as mimeo copies, flip-charts, and flannel boards. Then came opaque projectors, slides and 8mm film (and the habit of carrying an extension cord and an extra bulb). There was a lot of clanking and whirring in those days. And the focus was on "equipment."

Today's presentation technology is so electronically sophisticated as to be nearly incomprehensible. However, it is actually designed to hark back those simpler times and provide an easy-to-use interface and offer a dramatic, mind-grabbing experience for the audience vis-a-vis the material being presented. Today, the focus is back on the information; the medium is becoming invisible.

This third in a series of special section on how business uses the new technology deals with some of the new "transparent" presentation products that can help you communicate faster, more effectively, and more persuasively to large groups as well as small.

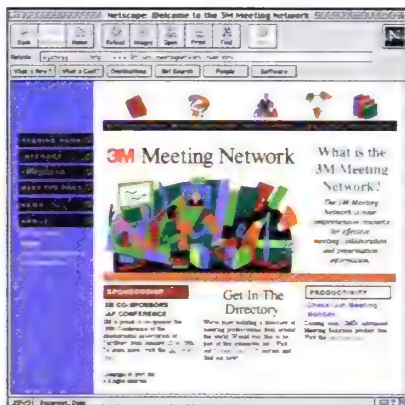
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Here's a quick overview of what you'll find at the site:

3M Meeting Guides: useful tips and information on how to conduct a better meeting using a variety of meeting tools

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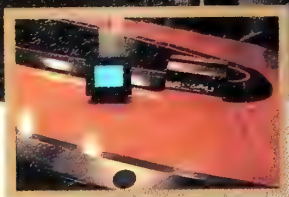
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Deloitte & Touche is an example of today's corporate



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presentation challenges and the solutions provided by remote control systems such as those manufactured by **Crestron Electronics**:

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For the audio distribution, microphones and speakers were designed into the conference table. Completely invisible, but very functional. Using advanced electronics, each person seated at the boardroom table hears the others as if they were sitting in the next chair. This audio equipment is

integrated with the videoconferencing equipment, allowing clear communication from any seat in the room for global meetings.

Now for those Power Point demos: stopping a meeting each time someone needs to make a laptop presentation is just not practical at D & T. Again, the consultant came up with a winning idea: The boardroom table is wired so that each laptop connects directly to the projector via the appropriate computer-video interfaces. A touchpanel provides simple control of the entire room, including the laptop displays. Thanks to the wired table, anyone can make an electronic presentation with the touch of a button.

High-tech solutions for presentation challenges are endless. Today's state-of-the-art technology can make meetings and presentations functional and easy to put on. And using a/v consultants like **CMS**, located in N.Y., is a great way to ensure that the room will meet your company's needs — today and for years to come!

A "SOUND" SOLUTION FOR ATTENTION-GRABBING PRESENTATIONS

An integrated system from EIS.

Picture visiting St. Peter's Basilica, touring a region in Southwest France, or flying over the San Francisco Bay — all in one day. Or imagine an environment that allows users to manipulate and control their surroundings with the touch of a fingertip. Today, both are possible with a virtual reality system aptly called the Visionarium.

Silicon Graphics (SGI) in Mountain View, Calif., developed the Visionarium. It is used to show customers, educators, scientists and planners how they can create innovative solutions and solve intricate problems.

The Visionarium creates a virtual reality, three-dimensional environment that maximizes sensory experience by using the most advanced computer graphics, sound and audiovisual system design.

Similar to today's architectural computer programs, the Visionarium ventures to create real-time, full-motion, walk-through or fly-through of complex urban environments, for example, allowing the architects and planners to view specific materials with



The Visionarium, a Virtual Reality System by

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particular colors and textures. However, the Visionarium is able to provide these planners with an unrivaled combination of computer and graphic capabilities.



NEED TO PROJECT ON A BIG SCREEN BEFORE A LIVE AUDIENCE?

Here's the video
projector that turned
on Computer America.

Silicon Graphics collaborated with Studios Architecture and EIS (Electrical Integrated Solutions) to design and build the multimedia systems for the Visionarium. EIS was instrumental in solving complex problems encountered by SGI. For example, they needed a way to exhibit the computer's complex graphic capacity. The computer, known as the Onyx, is able to display 1280 x 1024 graphic resolution with full motion on three different simultaneous displays. In other words, one could sit at a radius of 18 feet away from the screen that almost completely surrounds the subject, thus giving a feeling of reality.

The main problem was how to enable a system beyond video capabilities so the customers would feel like they are there. EIS developed an audio solution and surround sound system. EIS customized a THX surround sound system that includes the small subwoofers attached to the seats. This then transferred low-frequency sound into vibrations that relate to the movement of the image.

EIS was instrumental in the design of the Visionarium. It created a unique presentation environment that is the ideal model for computer simulation systems. The project features a fully integrated audio, video/data, and digital control environment utilizing components from leading audio visual manufacturers.

Radio host Craig Crossman made his syndicated weekly radio talk show, *Computer America*, even more interactive three years ago by including an AOL simulcast.

During the three-hour Sunday broadcasts from Palm Beach Atlantic College in West Palm Beach, Fla., the live audience sits in a well-lighted auditorium watching host Crossman, his radio guests, and a 25-foot screen which displays the AOL chat room. As co-host Mark Lautenschlager interacts in real-time with chat members on his IBM ThinkPad 770 laptop, the typed words are projected on the screen via an **Epson PowerLite 7000XB** multimedia projector from the back of the auditorium.

"Because of our projector system, everyone can see what's going on, and we can talk about issues raised in cyberspace for our radio audience," said Crossman. "While we're on the air talking to our guest experts, or taking toll-free phone calls and audience questions, we all can see exactly what's happening in the chat room, which has added a whole new dimension to the radio show."

The brightness of the projector is critical because *Computer America's* live audience is sitting in a well-

lighted auditorium. "No matter how bright the room gets, the words or images projected across the auditorium to the screen must be clear enough to be read by all of us, as input from the chat room can be a key part of any discussion," said Crossman.

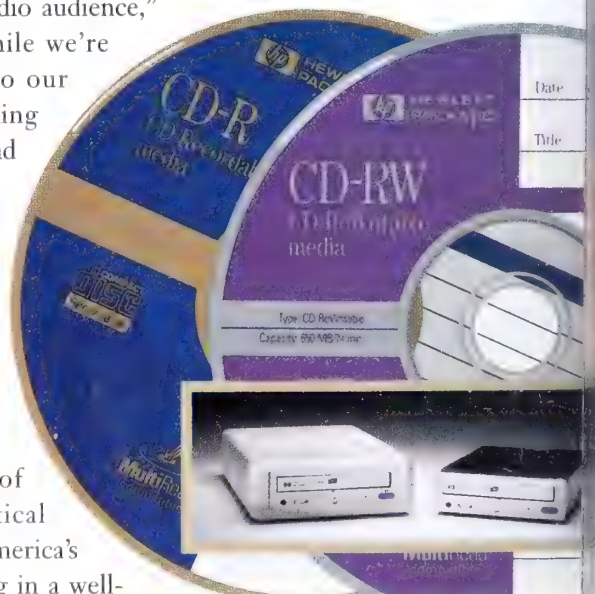
CAN CD-RW HELP MAXIMIZE YOUR PRESENTATION OPPORTUNITIES?

HP thinks it can.

In an era in which data production is increasing faster than hard drive capacities, developers of technologies such as re-writable CDs are extending users' abilities to store, manipulate, and share ever-greater amounts of data with the ease of floppy drives.

Wayne Brothers, president of **Teledyne Water Pik**, was looking for a better solution to deliver multimedia slide presentations to his sales force in the field.

Since the presentations contained graphics, digitized images, and sometimes videos, the files were often 1Mb or larger. In the past,



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Make the meeting

3M Innovation

They tried sending the large files through the phone lines, which sometimes took several hours. And, if there was ever a problem during transmission, the process had to be started all over again. "It wasn't very efficient," said Brothers.

"Now, we can quickly save the files onto a CD, and send them overnight to our sales force. The CD-RW allows us to easily share and transport impressive and very large visual presentations; we just couldn't do that before."

Brothers especially likes the read-write-erase capability of the CD-RW. "We're always tweaking these presentations right up to the last minute. With the CD-RW option, we can change or update the information without having to start completely over again," he said.

Brothers feels that the best features of the CD-RW are its flexibility and portability. "The opportunity to really refine our slide presentation before committing to it and having it stored in an easily transportable format really sold us the Hewlett-Packard Sure Store CD-Writer Plus."



TIRED OF TRYING TO DEMONSTRATE POINTS OVER THE PHONE?

The Interactive Factory may have your answer.

Pictures, animations, and product demonstrations can aid any presentation by allowing the audience to visualize your product by permitting you to show them how that product works.

The problem? In today's global business environment, it can be difficult and extremely expensive to coordinate face-to-face meetings with your clients, colleagues, and employees. You might have to schedule a meeting for several weeks down the line, pay for an expensive plane ticket and then hope that all the right people, especially the decision makers, are in the same room at the same time to hear your message.

The **Interactive Factory**, a Boston-based technology company, has developed a solution to these presentation problems. Their answer is an innovative product called *Driver*, a software package that leverages technology already existing on most of today's desktops and gives you, the presenter, temporary control of your audience's Web browser. With *Driver*, you can provide dynamic visuals on the monitor while talking with your audience over the phone.

Using the Internet, *Driver* creates a visual presentation 'channel' between you and your audience. It can be used by a sales rep with prospects or customers, by a manager with trainees, by an educator with a group of students, or by a group of colleagues. *Driver* can be used to reach anyone who would benefit from the presentation, provided that your audience has a phone and an Internet connection.

For example, when calling a prospect, a sales rep explains that he or she can demonstrate the product over the phone. The prospect opens up their Web browser and types in the security password given to them over the phone. A window appears on their computer screen. This is the sales rep's film/slide projector.

From here, the sales rep can take control of the presentation and show the customer exactly what they should see.

Although *Driver* may not fit in every presentation situation, it can be ideal in many applications.

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WHAT'S THE BEST WAY TO PROJECT PRODUCT DEMONSTRATIONS?

And make on-the-road demos easy, too?

Dun & Bradstreet's Ron DeBlis and his sales colleagues in the company's Supplier Evaluation and Management Services organization wanted an easy yet professional solution to this challenge. D & B is a world leader in providing global business infor-

mation solutions. Their new software, named "Supplier Assessment Manager" (SAM), allows purchasing professionals to manipulate D & B information integrated with their supplier information to gain insight into their own supplier bases.

"Before, we primarily used a PC viewer on top of an overhead projector," DeBlis said. "The clarity and brightness were absolutely terrible. And for many laptops, it wasn't even compatible."

Besides that, D&B needed to rely on customers to provide the right kind of overhead projector — in good working order and in the right room — along with a screen. In short, there were any number of potential fracture points, even before a presentation could get underway.

To avoid these problems when demonstrating the new software, D&B has purchased 11 **Sharp NoteVision** multimedia LCD (liquid crystal display) projectors.

In addition, the NoteVision projector is compatible with a wide range of PC and Macintosh computers. It can also connect to a video source, such as a VCR, eliminating the need for a TV monitor during a presentation. "The stereo sound system is superior to the competition," according to George Meglio, sales manager for the dealer that sold D & B the machines.

Dynamic sales presenters like to walk as they talk — and the NoteVision's wireless, remote control makes that possible. "It's wonderful. You get to walk around the room and really be interactive with the customers, instead of sitting behind the notebook," DeBlis said. A built-in mouse and laser pointer puts the presenter in total control from anywhere in the room.

And what if a few extra people show up unexpectedly for the demonstration? That's no problem from an equipment point of view, because the NoteVision's zoom lens projects an image from 30 to 300 diagonal inches. You don't even need a screen when a white wall is available. "This enables all the people in the room to see it and to understand the functionality of our software, so it really does facilitate the sales call," DeBlis said.

Besides being the perfect partner during a sales presentation, Sharp's NoteVision projector is a hassle-free companion en route to the event. The whole package fits under an airline seat or in an overhead compartment.

IS THERE A LARGE FORMAT MONITOR VIEWABLE IN BRIGHT LIGHT?

Consider Plasmavision technology.

Fujitsu General America now offers Plasmavision™ 42EP, a second-generation big-screen, flat-panel plasma display, which features a new high-contrast screen that delivers a major improvement in contrast levels, for performance comparable to any display technology currently available.

In fact, one leading news wire service is using Fujitsu Plasmavision monitors to gain a competitive edge in that fast-paced market. The flat-panel displays are helping create high-impact presentations in a space that showcases the unique qualities of this exciting new technology.

The sales department of this business-news wire service was investigating ways to demonstrate its software to potential customers. This required a presentation device that could display computer input. The challenge was to find a technology

that worked in small rooms that often receive direct sunlight.

Plasmavision monitors mounted to the wall minimize the amount of precious space dedicated to the presentation device. The flat-screen displays allow wide viewing angle (up to 160°), so everyone in the room was certain to have a perfect view. In addition, since the monitors produce their own light, the display is viewable in the high ambient light conditions common to the wire service's offices.



Plasmavision technology by Fujitsu

Plasmavision 42s are now installed in all of the company locations and future plans include using the displays for video conferencing.

With a depth of less than 5 inches, the display is slim enough to hang on a wall, making it useful for business presentations, entertainment centers, and public display applications such as kiosks and promotional signage.

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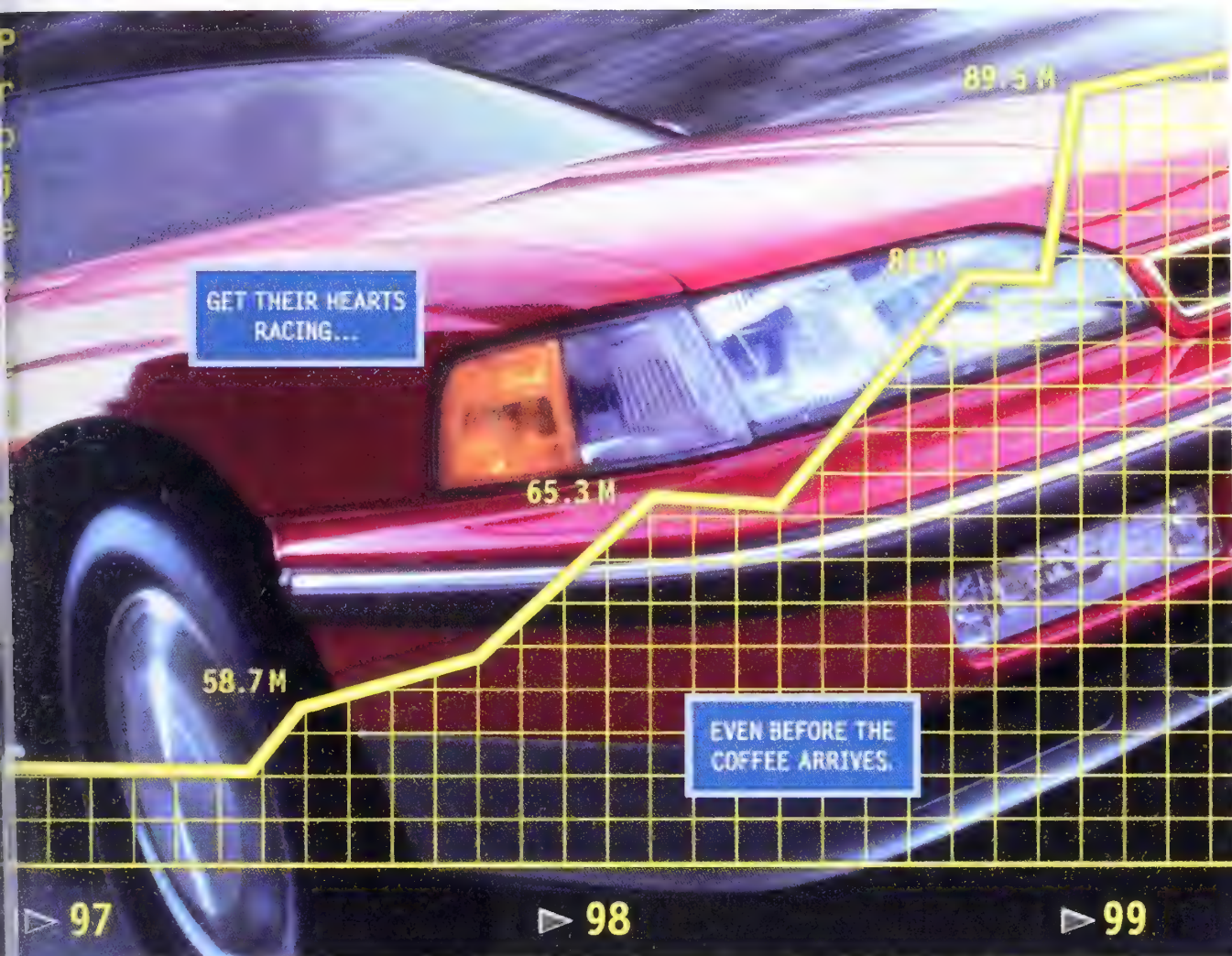
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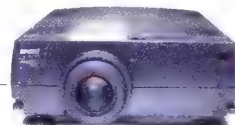
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PowerLite™ 7300



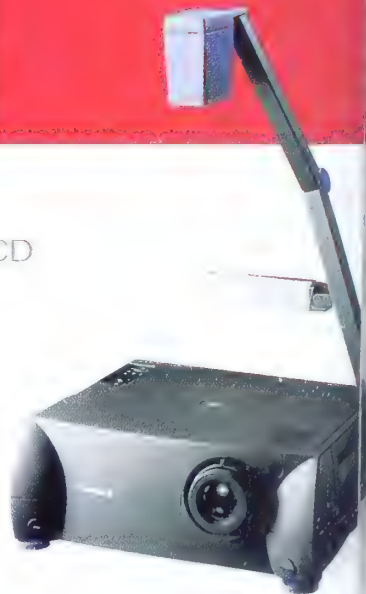
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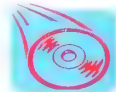
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COMMENTARY

By Karen Pennar

SHOULD UNCLE SAM POUR MORE BUCKS INTO SCHOOLS?

Ready, class? Sharpen your No. 2 pencils and answer a few simple questions about the state of public education in America.

Reducing class size will:

- a. Improve children's test scores
- b. Have no effect on performance
- c. Both of the above

Students' test scores:

- a. Have risen over the past 20 years
- b. Rank low internationally
- c. Both of the above

The U.S. economy's world-beating performance:

- a. Has nothing to do with test scores
- b. May fade as overseas students excel
- c. Both of the above

If you answered "c" to all three questions, congratulations! You have a handle on how difficult it is to evaluate America's educational system. Dozens of academic papers have been written on the subject of class size, and studies have been conducted from Connecticut to Tennessee. Yet little consensus has been reached. Experts agree about whether the glass is half empty or half full. Wags look at America's high-tech and information industries have led a productivity and growth revival that is the envy of the world and wonder: If we're so smart, how come we're so rich?

Given this degree of clarity, it hardly seems time to ramp up education spending. Yet President Clinton wants

Education Dept., always a small player in the funding of elementary and secondary-school education, to find an additional \$2.2 billion in five-year 1999 on initiatives such as reducing class size for grades 1 to 3 and moting technology in the classroom. Republicans are threatening to kick away at the request.

There are good reasons to question more spending. Over the past 30 years, spending per student—the bulk of it locally financed—has more than doubled in real terms, to a nationwide average of \$6,500, helping push the pupil-teacher ratio down from 24 to a shade over 17. Mean-

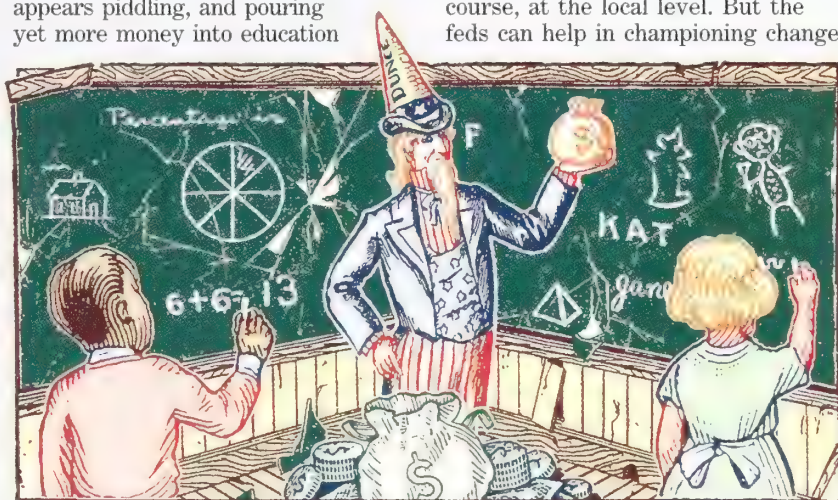
while, after improving in the 1960s, national assessments of reading, writing, mathematics, and science plunged in the '70s and early '80s, only to recover slightly in recent years. And on recently released international tests, U.S. 12th-graders fared poorly against many Northern European and East Asian students.

So the payoff from that spending appears piddling, and pouring yet more money into education

those students now outperforming U.S. kids could give their nations' businesses a big edge in the global sweepstakes.

Or maybe not. Maybe those intangibles of American success, such as creativity, openness, and flexibility, will make the difference. But why gamble? Why not try to raise scores?

Improvements have to happen, of course, at the local level. But the feds can help in championing change,



It's not clear that big spending to cut class size makes any difference. But the feds can fund smart research that will point the way

would seem like folly. Yet it's not that simple. There are long lags between the time reforms are adopted and results are detected. And it's often in the workplace, not in exam rooms, that the payoff becomes clear. Students who hit the books and buoyed their math scores in the 1960s are in their 40s, managing corporations. They completed more schooling and were more likely to go on to college than the previous generation, and now are earning a higher return on their efforts.

That trend toward more years of schooling is catching on. In Europe, a university education is no longer just for the elite, and students are well-prepared in secondary schools. That's what makes the international test results troubling: In 10 to 20 years,

especially by sponsoring well-designed experiments to learn which reforms truly work. Rather than finance a nationwide reduction in class size as President Clinton has proposed, the Education Dept. should fund more and better tests of the impact of smaller class size. Or, as Princeton University economist Alan B. Krueger suggests, other "incremental reforms," such as a longer school year, after-hours programs, and summer programs could be tried and studied. These initiatives needn't be as costly as the current budget requests. But they could play a big part in leveraging meaningful reform at the grass roots.

Senior Writer Pennar covers education and economics.

EDITED BY AMY DUNKIN

CAVEAT INVESTOR AT THESE SEMINARS

When Bell Atlantic offered Bud Aro an early retirement deal, the Timonium (Md.) engineer decided he should brush up on his financial-planning knowhow. So he enrolled at nearby Towson University in a seminar on managing personal finances. The instructor, a local planner, impressed him enough that Aro signed up for the optional consultation offered as the course's final session. Now, three years later, Aro thinks that was a mistake. "What I didn't know at the time was that this guy only deals with [load] mutual funds, and some of them are expensive," he says. "I could've done better with no-load funds, but he doesn't talk about them."

Each year, thousands of other "students" fall into the same trap. The problem is the course Aro took was designed not by any professor paid by Towson but by Successful Money Management Seminars. Since 1985, The Tualatin (Ore.) company has built a 2,100-member network of brokers, insurance agents, and other financial-services providers who use SMMS materials to run seminars, often sponsored by companies and nonprofits—even by universities as prestigious as Notre Dame. Last year, 230,000 families attended the sessions. **SOFT SELL.** By themselves, these courses don't make the broker-instructor any money. The tuition, \$59 or so for a three- or four-session course, goes to SMMS for workbooks and to the college or other sponsor for registration and classroom costs. So why do they bother? Because the

brokers hope to convert students or "buying units" into paying clients. "For every body that I put into the chair, it's worth about \$1,500 to me in my pocket," boasts one instructor on an SMMS promotional tape aimed at brokers.

Brokers and other professionals, such as tax and estate attorneys, routinely offer lectures on their specialties to keep their name before the public and, by extension, win clients. But there, the interests are plain and the nature of the soft sell readily understood. By contrast, in these college-sponsored seminars, the sales pitch often is obscured, sometimes with the college's encouragement.

When I phoned Florida Institute of Technology (FIT) recently to inquire about its seminar, the first thing I heard was: "It's not a selling thing." And sometimes, as at Towson and FIT, the brokers mail brochures with the sponsor's nonprofit postal permit, making no mention of the teacher's identity. So it may not be until students have paid the fee and attended a session that they learn who the instructor is, how he makes a living, and how superficial the university's role is. SMMS says it advises brokers not to use nonprofit mailing permits.

Soliciting students without disclosing a broker's identity and affiliation would violate National Association of Securities Dealers rules governing how brokers may communicate with the public, spokeswoman Nancy Condon confirms. But the NASD has taken no action against SMMS or its network members. A

seminar "is a helpful sales pitch, but it is a sales pitch nonetheless," observes Robert Karoly, a securities arbitration expert and author of *The Empowered Investor* (Dearborn Financial Publishing; \$19.95). "Otherwise, no one has anything to gain. What [the broker-teacher] is getting is your confidence."

Colleges, the brokers, SMMS, and its parent, ReliaStar Financial, a \$2.5 billion Minneapolis-based insurance and securities conglomerate, stress the unbiased nature of the curriculum, which doesn't endorse any product or firm. "The curriculum is extremely generic," says ReliaStar President John Flittie.

But to the financial pros it solicits to join its network, SMMS stresses something else. "Imagine the credibility and prospecting power you will achieve," one brochure suggests, "when corporations, universities and community colleges, organizations, and



churches sponsor your seminars." Sponsors, Flittie says, are "quite endorsing [the brokers] but they're coming awfully close to it."

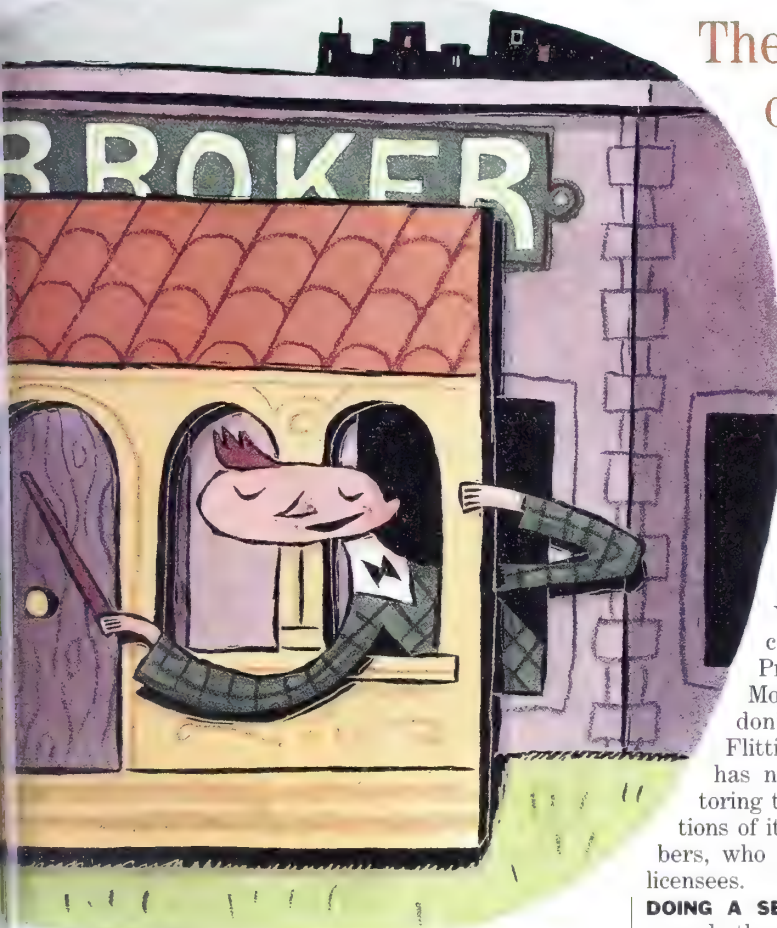
Nor does anyone make bones about the fact that brokers use the seminar to sell themselves. A video describes how for "the break during session is an important time... you begin building

ADVICE WITH NO SNAKE OIL

If you want to learn more about investing and financial planning, there's no shortage of free seminars on everything from stock-picking

to money management for women. But most are not by neutral investors but by brokers: mutual-fund companies would like you as a

Most course sponsors hide who they are. And because the instructor is a broker for the firm, you mean the information. But you'll likely be led to a soft sales pitch.



The sales pitch is often obscured in finance courses sponsored by colleges

annuities, and other investments that carry sales charges. Does the curriculum also cover the cheaper varieties of funds and annuities called no-loads?

Yes, says SMMS co-founder and President Douglas Mortensen, but "we don't dwell on it."

Flittie says ReliaStar has no way of monitoring the recommendations of its network members, who are independent licensees.

DOING A SERVICE. Colleges concede they're trading away part of their cachet, but they say the seminars are highly popular and, as long as there's no hard sell, legitimately meet a public hunger for help in managing finances. "We are essentially doing this as a service to the community," says Ronald Marshall, dean of FIU's School of Extended Graduate Studies. Asked why brochures don't disclose the instructor's identity or aims, he says, "I don't want to destroy the

credibility of the professor... It would add a dampening effect."

Jennifer Kafka Smith, Towson's assistant director of corporate, executive, and extended education, says the program has generated few, if any, complaints over many years. "I don't view [the broker-teachers] as being wallet chasers," she says. Notre Dame's director of continuing education, Peter Lombardo, hopes it helps that brochures going out with Notre Dame's imprimatur include the instructor's name and affiliation, even if it is in tiny print. "I would much prefer our own faculty do these things," he says. "We just try to offer it as an informational program and do the best we can not to let it disintegrate."

Looking back, Bud Aro wishes his broker-teacher had simply left alone the two no-load funds he already owned, instead of replacing them with funds that levied sales charges. "I had never been exposed to this world where people are selling their services" in the classroom, he says. "I haven't lost money necessarily, but I could've done better." *Robert Barker*

ort with
idual prospects." Also,
the first session, they
out "homework" called a
nal financial data form—
industry's most popular
effective client informa-
gathering tool," says an
brochure. The form, the
explains, "requests con-
tial information, which
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nation they provide will

enable you to
prepare an appropriate and
thorough financial plan and
to justify your recommenda-
tions.... It also preconditions
them to take action later at
the personal plan review and
consultation."

Because most of the in-
structors operate at least
partly on commission, any
prospect who attends the
personal consultation is likely
to hear about mutual funds,

to these seminars
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g the willpower to
ays Robert Veres,
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which organizes
1,200 sessions a
nominal fee of less

than \$25 per person. The cur-
riculum focuses on the nuts
and bolts of stock-picking,
and the goal is to make you a
do-it-yourself investor. In-
structors are NAIC-trained
members who often spend
some time expounding on the
merits of investment clubs.
Likewise, the American Asso-
ciation of Individual Investors
(800 428-2244) runs day-long
seminars for \$150, taught by

finance professors who aren't
fishing for clients. The AAII
assumes participants have an
intermediate knowledge of
the markets and will eventu-
ally use a stockbroker or fi-
nancial planner.

Before taking any course—
no matter who's behind it—
ask about the instructor's
background, investment phi-
losophy, and expertise. Make
sure the instructor has a rec-

ognized professional creden-
tial, such as certified financial
planner or certified public
accountant. Don't expect
your specific needs to be
addressed. Courses are
taught to people of various
ages, incomes, and financial
goals. So don't waste your
time in a class if what
you want is one-on-one
attention from a financial
planner. *Adele Malpass*

MY TRIP THROUGH PC HELL

I may be computer-literate, but I recognize my limitations. So when it came time

to add a second hard drive to my Gateway 2000 Pentium, I asked a friend to handle the installation. Never mind that my new Western Digital drive was "easy to install." That's what the box said, anyhow. It took my pal four hours of flipping switches and connecting cables before the mission was accomplished. Or so we thought.

My new hard drive was a ticket to a PC hell that took me weeks to escape. The experience showed me how far the industry still has to go to deliver complete customer satisfaction. Sure, makers promise technical support. But some of the people who were supposed to help me at Gateway, for instance, dished out wrong or conflicting information. And the help they did provide was peppered with such technojargon as "bus mastering" and "BIOS."

INTERNET AID. At times, folks in trouble can get help via the Internet. Programs such as Oil Change, Norton Live-UpdatePro, and Tune-Up.com notify you of software updates and bug fixes available in cyberspace and can download the files onto your system. Utilities programs—including First Aid 98 from CyberMedia, Norton Utilities from Symantec, and Nuts & Bolts from Network Associates—can help curb system crashes. But I needed a live expert.

The first thing I no-

ticed after adding the drive was that my modem started misbehaving. I could use the device to dial America Online. But my computer thought the modem was already in use when I tried phoning Microsoft Network or CompuServe. I attempted to resolve the problem by visiting the support area at Microsoft's Web site (table). But the remedy prescribed did not work. The MSN techies I reached by phone were unable to resolve the issue, either.

That led me to my modem maker, Zoom Telephonics. After dispatching an E-mail via AOL, I got a quickie response that was of no help. When I reached a Zoom rep by phone, I was told the modem

was indeed working properly; it did, after all, dial AOL.

My frustration mounting, I got back on the horn to a Microsoft Windows 95 specialist. His kind of pay-per-incident support costs \$35. After a couple more hours exhausting various possibilities, Microsoft concluded the

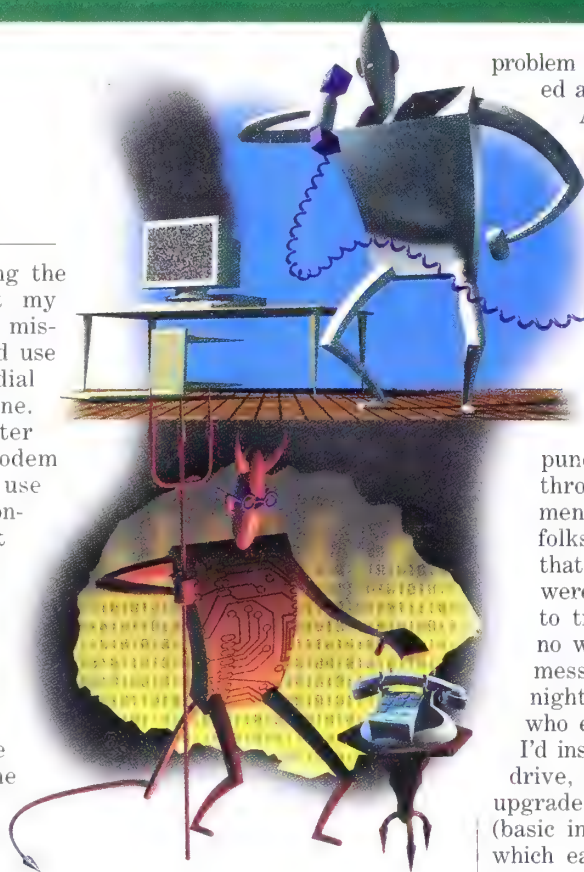
problem was hardware-related and beyond its realm. At least I was promised a refund.

Since the hard drive seemed to work okay, I avoided calling Western Digital and turned to Gateway. It offered toll-free technical support for as long as you own a machine.

I punched my way through a touch-tone menu only to have a folksy voice advise that all representatives were busy and I'd have to try later. There was no way to leave a voice message. Around midnight, I reached a rep who explained that while I'd installed the new hard drive, I should have upgraded the system BIOS (basic input-output system which eases the transfer of data between the PC and peripherals). I was advised to download an upgrade from the Gateway Web site.

BUS MASTERING? All seemed to go smoothly, save for an error message that indicated bus mastering was not supported. I wasn't sure what that meant, so it was back to Gateway, where another rep told me there was a problem. I could download the BIOS, but it would take care of things. Big mistake. The CD-ROM went on to blink, and when I tried to reinstall it, my system crashed.

Gateway's befuddled rep couldn't figure out how to revive the system. My case, he informed me, would have to be "escalated" to hardware specialists. I was told to expect a call back two nights later. It never came. When I complained, another rep told me such a promise couldn't have been made and the 24-hour period in which I was supposed to go



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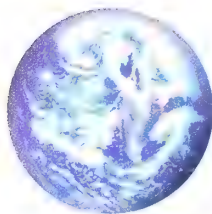
COMMENTS

Online troubleshooters download bug fixes for any system and software; TuneUp from Quarterdeck provides similar service

Members who call the help center get priority treatment for the first year, also free software downloads and E-mail to keep system running smoothly

Pentium users who submit questions via the Net are promised a callback in minutes; service also provides virus protection, online backup for files, tips

Lets you search free online database for problem solutions before seeking live help; tech support prices vary by product and time of call



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return call wasn't over. He insisted the call would come the following evening. Yeah, right. When I reached a rep the following week, he instructed me to flip a jumper switch on my motherboard, which let me boot up. But during the next few days, my system repeatedly crashed. So Gateway recommended I back up files and reformat my drives.

But when I called Gateway to walk me through the reformatting process, a rep claimed the CD-ROM that came with my system might cause

problems if I tried to reinstall everything. He said Gateway might have to ship me a new CD-ROM, but such a decision would have to come from a hardware specialist. Then I got lucky. Another rep suggested I try reformatting the hard drive, after all. I did, and everything finally ran perfectly.

When I told my tale to the head of Gateway's tech-support, he apologized and explained that I'd hit the company during its busiest season—after Christmas. Meanwhile, Gateway is work-

ing on diagnostic tools to be shipped with future systems to intercept potential conflicts before they cause damage.

What should you do if you find yourself in PC hell? If you can wait out a problem, you might try calling help lines during off hours or on weekends—Mondays are busy. Many companies provide premium support for a price. For \$99, Gateway will give you an extra two years of onsite service (on top of the year that comes with its systems) plus a toll-free phone number that gives you

quicker access to a tech rep. New Packard Bell PCs come with software to diagnose problems and prevent users from accidentally deleting files. Intel Answer Express provides help for leading software titles. But snafus remain an unfortunate part of the PC experience. Tom Rhinelander, an analyst with Forrester Research, jokes that computers should carry warning labels. "This device is complicated, has a tendency to crash and explode." I found out the hard way. *Edward C. Ba*



GIVING A BOOST TO AGING BONES

Mimes stoop when they portray an elderly person. But age doesn't cause stooping; fractured vertebrae brought about by osteoporosis does. This degenerative bone disease is preventable and treatable if caught early. The good news: A recent advance in screening technology

and updated dietary guidelines can help keep more older people standing tall.

In March, the Food & Drug Administration approved the first ultrasound device that measures bone density—a key to diagnosing osteoporosis. Called Sahara and manufactured by Hologic in Waltham, Mass., it's considerably smaller (about the size of a laser printer) and

half the price (\$30,000) of other measurement devices. And it doesn't use X-rays.

The exam requires you to slip a bare foot into the device, allowing sound waves to pass painlessly through your heel. The machine prints out results within a minute, at a cost of around \$40, vs. more than \$100 for other types of bone scans, which take 10 minutes or more. And "Sahara is just as accurate" at determining who is at risk, says Dr. Daniel Schultz, chief medical officer in the FDA's Device Evaluation Div. Health insurers are expected to pick up the tab for the test.

In the past, only large medical centers had the resources for scanning gear. But a Sahara scanner can be

installed in any physician's office.

(Call 800 330-0927 for existing locations.) Dr. Felicia Cosman, an osteoporosis specialist at Helen Hayes Hospital in West Haverstraw, N.Y., thinks osteoporosis screening "will become part of any standard health evaluation," along with height, weight, and blood pressure.

This is important because most people start to lose bone mass after age 30. But some deplete bone stores faster than others. Women can lose up to 20% in the several years following menopause, when estrogen levels fall. With a 25% loss, bones become brittle. In the

worst cases, sneezing is enough to break a rib.

Fortunately, "if people find they are rapidly losing bone mass, they can take steps to arrest the process before they start having fractures," says Gail Dalsky, a researcher at the Osteoporosis Center at the University of Connecticut Health Center in Farmington. Treatment includes hormone-replacement therapy, drugs that slow bone loss, and weight-bearing exercise, such as walking, aerobics, and weight-lifting.

It's also vital to get enough calcium, a mineral crucial to sustaining a healthy skeleton. Last year, the National Academy of Sciences' Institute of Medicine upped its recommended dose after an expert panel concluded that men aged

HEALTH

women need 1,000 to 1,500 milligrams of calcium per day—a 50% hike over the last recommendation in 1980.

Doctors advise getting calcium from foods because they supply other nutrients that aid in absorption. But chances are you don't consume enough dairy products, kale, and other calcium-rich foods. So experts suggest taking calcium citrate, which has a higher absorption rate than calcium phosphate and calcium carbonate. To maximize efficiency, take 500 mg at a time. You might have to pop a few pills a day, but it's a small price to pay to keep your head high. *Kate Murphy*

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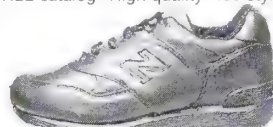
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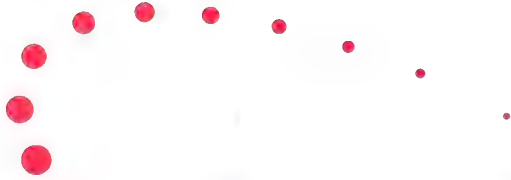


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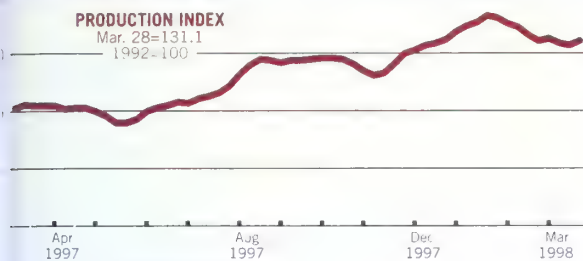
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Business Week Index

PRODUCTION INDEX

Change from last week: 0.3%
Change from last year: -4.5%



production index was up in the week ended Mar. 28. The unaveraged index also up, to 131.7 from a revised Mar. 21 figure of 130.9. After seasonal adjustment, auto and truck production both rose, and the sharp gain in mobile shipments helped to push U.S. rail-freight traffic up by 2.6%. Steel output increased with the rate of capacity utilization at a high 92.6%. All other ponents were down. The monthly index for March was unchanged at 131.1.

Source: U.S. index, copyright 1998 by The McGraw-Hill Companies

ADING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
CK PRICES (4/3) S&P 500	1122.70	1095.44	48.1
PORATE BOND YIELD, Aaa (4/3)	6.67%	6.69%	-13.5
IEY SUPPLY, M2 (3/23) billions	\$4,122.7	\$4,122.8r	6.6
IAL CLAIMS, UNEMPLOYMENT (3/28) thous.	309	314r	-0.6
ITGAGE APPLICATIONS, PURCHASE (4/3)	248.8	222.2	43.0
ITGAGE APPLICATIONS, REFINANCE (4/3)	1,206.3	1,297.1	312.7

ces: Standard & Poor's, Moody's, Federal Reserve, Labor Dept., Mortgage
ers Assn. (Index: March 16, 1990=100)

TEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
ERAL FUNDS (4/7)	5.40%	5.88%	5.34%
MERCIAL PAPER (4/7) 3-month	5.45	5.50	5.69
IFICATES OF DEPOSIT (4/8) 3-month	5.56	5.60	5.70
D MORTGAGE (4/3) 30-year	7.23	7.17	8.30
STABLE MORTGAGE (4/3) one-year	5.79	5.77	6.04
IE (4/3)	8.50	8.50	8.50

ces: Federal Reserve, HSH Associates, Bloomberg Financial Markets

data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense
ment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

IL SALES

ay, Apr. 14, 8:30 a.m. EDT ▶ Retail likely rose just 0.2% in March, according to the median forecast of economists surveyed by Standard & Poor's MMS, one of The McGraw-Hill Companies. Sales increased by 0.1% in February. Excluding cars, store sales were probably up 0.1% on top of a 0.2% advance in February.

UMER PRICE INDEX

ay, Apr. 14, 8:30 a.m. EDT ▶ Consumer price index for goods and services likely rose in March. Excluding food and energy, the index likely rose 0.2%. In February, the index edged up 0.1%, while higher service prices lifted the core index by 0.3%.

BUSINESS INVENTORIES

Wednesday, Apr. 15, 8:30 a.m. EDT ▶ Stockpiles held at factories, wholesalers, and retailers probably increased 0.3% in February, after no change in January.

HOUSING STARTS

Thursday, Apr. 16, 8:30 a.m. EDT ▶ The S&P MMS survey projects that housing starts likely fell to an annual rate of 1.58 million in March after rising 6% in February, to a 1.64 million pace.

INTERNATIONAL TRADE

Friday, Apr. 17, 8:30 a.m. EDT ▶ The trade deficit of goods and services was probably little changed in February from January's

large \$12 billion. Both exports and imports probably held steady in February after each sector fell in January. The dollar value of all imports was probably held down by falling oil prices.

INDUSTRIAL PRODUCTION

Friday, Apr. 17, 9:15 a.m. EDT ▶ Output at factories, mines, and utilities was probably flat in March, says the S&P MMS forecast. If so, that will be the second month of no change in output. The decline is suggested by the drop in hours worked in the factory sector. The softness in production suggests that the average operating rate for all industry likely slipped to 82.5% in March, from 82.7% in February.

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (4/4) thous. of net tons	2,218	2,246#	3.2
AUTOS (4/4) units	119,460	127,185r#	7.8
TRUCKS (4/4) units	151,907	148,592r#	32.2
ELECTRIC POWER (4/4) millions of kilowatt-hrs.	58,695	59,649#	5.3
CRUDE-OIL REFINING (4/4) thous. of bbl./day	14,641	14,601#	2.1
COAL (3/28) thous. of net tons	22,103#	21,902	-0.5
LUMBER (3/28) millions of ft.	476.0#	481.6	-2.1
RAIL FREIGHT (3/28) billions of ton-miles	27.6#	27.0	3.4

Sources: American Iron & Steel Institute, Ward's Automotive Reports, Edison Electric Institute, American Petroleum Institute, Energy Dept., WWPAl, SFPaZ, Association of American Railroads

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (4/8) \$/troy oz.	308.800	301.000	-11.2
STEEL SCRAP (4/7) #1 heavy, \$/ton	134.50	135.50	-1.5
COPPER (4/3) ¢/lb.	80.9	82.4	-29.7
ALUMINUM (4/3) ¢/lb.	68.8	69.5	-12.4
COTTON (4/4) strict low middling 1-1/16 in., ¢/lb	65.17	67.44	-5.3
OIL (4/7) \$/bbl	14.93	15.33	-21.6
CRB FOODSTUFFS (4/7) 1967=100	228.54	229.17	-6.2
CRB RAW INDUSTRIALS (4/7) 1967=100	298.39	300.51	-10.6

Sources: London Wednesday final setting, Chicago market, Metals Week, Memphis market, NYMEX, Commodity Research Bureau

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (4/8)	132.19	133.75	126.74
GERMAN MARK (4/8)	1.82	1.85	1.72
BRITISH POUND (4/8)	1.67	1.67	1.62
FRENCH FRANC (4/8)	6.09	6.21	5.80
ITALIAN LIRA (4/8)	1794.5	1826.8	1699.3
CANADIAN DOLLAR (4/8)	1.42	1.42	1.39
MEXICAN PESO (4/8) ³	8.510	8.505	7.884
TRADE-WEIGHTED DOLLAR INDEX (4/8)	110.8	111.5	106.6

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars. Trade-weighted dollar via J.P. Morgan

This Week, Online

Business Week presents frequent live conferences and chats on America Online—your opportunity to ask questions about timely topics.

Sunday

Kevin Bailey, co-author of *Customer Service for Dummies*, talks about—what else?—how to make customers happy. **Apr. 12**
9 p.m. EDT in BW Online's Conference Room

Thursday

How do you pick a stock in today's hot market? Robert S. Natale, VP and director of equity research for Standard & Poor's, will satisfy your curiosity. **Apr. 16**
9 p.m. EDT in BW Online's Conference Room

B-Schools

MBA students answer questions about campus life. **Apr. 14: Virginia**
Apr. 16: Dartmouth
8 p.m. EDT in the BW Online Chat Room
AOL keyword: BW Talk

Transcripts of all conferences are available for downloading from the BW Online area on AOL soon after each event.

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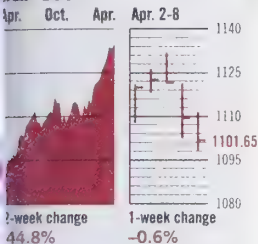


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Investment Figures of the Week

STOCKS

S&P 500



COMMENTARY

U.S. markets continued their record-breaking gains—for a while, at least. The Dow Jones Industrial average pierced the 10,000 barrier on Apr. 6, when it closed above that number for the first time, ending the day at 10,013. The rally was spurred by word of a planned merger of Time Warner Group with Citicorp. But the euphoria faded, so did the rally, and the market gave up 100 points over the next two days. Concern about corporate earnings also fueled the decline. The dollar sagged against the yen and the German mark.

U.S. MARKETS

	Latest	% change Week	% change Year
Dow Jones Industrials	8891.5	0.3	35.5
NASDAQ Combined Composite	1807.0	-2.2	44.6
S&P MidCap 400	366.8	-1.5	43.7
S&P SmallCap 600	198.1	-2.4	41.7
S&P SuperComposite 1500	235.9	-0.8	44.6

SECTORS

	Latest	% change Week	% change Year
Bloomberg Information Age	331.8	-2.6	43.4
S&P Financials	136.7	2.9	57.8
S&P Utilities	244.5	-0.7	31.7
PSE Technology	339.5	-3.5	35.3

FOREIGN MARKETS

	Latest	% change Week	% change Year
London (FT-SE 100)	6055.2	0.6	41.1
Frankfurt (DAX)	5269.5	2.2	56.9
Tokyo (NIKKEI 225)	16,376.6	0.8	-7.5
Hong Kong (Hang Seng)	11,314.5	-0.1	-9.0
Toronto (TSE 300)	7571.1	0.6	30.6
Mexico City (IPC)	4921.2	-1.6	29.6

FUNDAMENTALS

	Latest	Week ago	Year ago
S&P 500 Dividend Yield	1.40%	1.41%	1.92%
S&P 500 P/E Ratio (Last 12 mos.)	27.9	27.8	20.1
S&P 500 P/E Ratio (Next 12 mos.)*	21.8	21.5	16.0
First Call Earnings Surprise*	1.53%	NM %	5.25%

TECHNICAL INDICATORS

	Latest	Week ago	Reading
S&P 500 200-day average	968.6	963.0	Positive
Stocks above 200-day average	66.0%	66.0%	Neutral
Options: Put/call ratio	0.53	0.53	Negative
Insiders: Vickers Sell/buy ratio	2.64	2.62	Negative

Data: Bloomberg Financial Markets; *First Call Corp.

BEST-PERFORMING GROUPS

	Last month%	Last 12 months%
Pollution Control	20.3	Broadcasting 113.4
Gold Mining	17.6	Homebuilding 102.2
Invest. Banking/Bkrgr.	17.4	Specialty Appar. Retailers 93.3
Office Equip. & Supplies	16.3	Invest. Banking/Bkrgr. 93.0
Money Center Banks	12.7	Personal Loans 87.1

WORST-PERFORMING GROUPS

	Last month%	Last 12 months%
Tobacco	-11.2	Metals -25.0
Manufactured Housing	-9.6	Shoes -22.2
Toys	-8.3	Engineering & Constr. -13.1
Shoes	-6.2	Photography/Imaging -12.6
Metal & Glass Containers	-5.1	Gold Mining -11.6

BLOOMBERG MONEY FLOW ANALYSIS

Rebound ahead? Stocks with most significant buying on price weakness

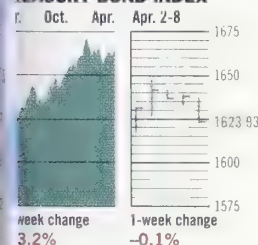
	Price	1-month change
Lockheed Martin	112 7/8	-3 1/8
Electronic Data Systems	43	-1/16
Delta Air Lines	115	-3 15/16
Telebras-ADR	123	-3 3/16
Micron Technology	28 1/16	-5 7/16
Sears Roebuck	55 3/4	-2 1/16

Decline ahead? Stocks with most significant selling on price strength

	Price	1-month change
Microsoft	87 1/4	7 21/32
WorldCom	42 3/4	4 1/4
Pfizer	100 19/16	13 15/16
Cisco Systems	69	7 23/32
PeopleSoft	52 1/4	4 7/8
Centocor	42 3/8	5 1/2

INTEREST RATES

TREASURY BOND INDEX



Bloomberg Financial Markets

KEY RATES

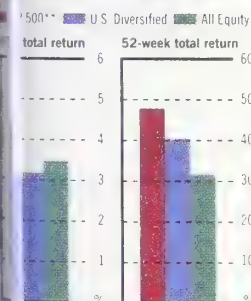
	Latest week%	Week ago%	Year ago%
MONEY MARKET FUNDS	5.11	5.11	5.02
90-DAY TREASURY BILLS	5.04	5.12	5.24
6-MONTH BANK CDS	5.06	5.05	5.13
1-YEAR TREASURY BILLS	5.29	5.37	5.98
10-YEAR TREASURY NOTES	5.57	5.62	6.91
30-YEAR TREASURY BONDS	5.89	5.90	7.11
LONG-TERM AA INDUSTRIALS	6.46	6.45	7.61
LONG-TERM BBB INDUSTRIALS	6.92	6.93	7.96
LONG-TERM AA TELEPHONES	6.75	6.74	7.82

BLOOMBERG MUNI YIELD EQUIVALENTS

Taxable equivalent yields on AAA-rated, tax-exempt municipal bonds, assuming a 31% federal tax rate.

	10-yr. bond Latest week	10-yr. bond Last week	30-yr. bond Latest week	30-yr. bond Last week
GENERAL OBLIGATIONS	4.43%	4.45%	5.03%	5.05%
PERCENT OF TREASURIES	80.32	78.63	86.24	85.02
TAXABLE EQUIVALENT	6.42	6.45	7.29	7.32
INSURED REVENUE BONDS	4.57	4.59	5.22	5.24
PERCENT OF TREASURIES	82.86	81.10	89.50	88.22
TAXABLE EQUIVALENT	6.62	6.65	7.57	7.59

MUTUAL FUNDS



Morningstar, Inc.

EQUITY FUNDS

Leaders		Laggards	
Four-week total return	%	Four-week total return	%
Lexington Strat. Invmtts.	22.8	DFA Japanese Small Co.	-13.4
USAA Gold	17.0	Lexington Troika Russia	-9.7
American Heritage	16.7	Capstone New Zealand	-9.7
Fidelity Sel. Prec. Mets.	15.9	Barr Rosenberg Japan Instl.	-8.2
Gabelli Gold	15.7	GMO Japan III	-8.1
Leaders		Laggards	
52-week total return	%	52-week total return	%
Delaware Aggressive Gr. A	87.9	U.S. Global Investors Gold	-52.8
FMI Focus	85.4	Matthews Korea I	-50.2
Munder Micro-Cap Equity Y	81.9	Midas	-48.1
Safeco Growth No Load	80.4	Morgan Stan. Asian Grth. C	-46.5
Fidelity Select Brokerage	79.1	Merrill Emerging Tigers B	-46.2

EQUITY FUND CATEGORIES

Leaders		Laggards	
Four-week total return	%	Four-week total return	%
Precious Metals	12.7	Japan	-4.4
Europe	7.4	Diversified Pacific/Asia	-2.1
Financial	6.0	Pacific/Asia ex-Japan	0.5
Foreign	5.8	Health	1.7
Communications	5.1	Technology	2.3
Leaders		Laggards	
52-week total return	%	52-week total return	%
Financial	57.8	Pacific/Asia ex-Japan	-30.8
Communications	56.6	Precious Metals	-26.8
Large-cap Growth	44.9	Diversified Pacific/Asia	-23.4
Unaligned	42.4	Japan	-10.3
Large-cap Blend	42.4	Diversified Emerging Mkts.	-7.8

are as of market close Wednesday, Apr. 8, 1998, unless otherwise indicated. Industry groups & S&P 500 companies only. Fundamentals, technical indicators, Bloomberg money flow analysis, and mutual fund returns are as of Apr. 7. For a more detailed explanation, write to us or E-mail figures@businessweek.com. NM=Not meaningful **Vanguard Index 500 Fund

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CITIGROUP: REALLY BIG MAY NOT BE BETTER

For sheer audacity, the Citicorp-Travelers Group Inc. merger is hard to beat. In one mammoth leap, the world of finance is forever changed. Punching through a welter of archaic laws, the giant \$70 billion Citigroup is a bold financial model for the global, digital age (page 37).

The goal, of course, is to offer everyone around the world a similar package of banking, investing, and insurance products they dearly need. Aging populations, privatizing pension programs, and booming stock markets are opening up global opportunities. The spread of the Net and digital technology provides the means of distribution. It all makes sense. Sort of.

The trends are real, but a colossal bank holding company may not be the optimum business model for the digital era. The Net is disaggregating all kinds of industries, allowing customers to get into direct contact with products. Why buy

stock insurance from Citigroup when an enormous variety of these products are available from the Net? Charles Schwab & Co. is already a kind of virtual brokerage. Some 30% of all stock trading is on the Net. Small or virtual may be as viable financial models in the 21st century as big. Maybe more.

Then there is the problem of who regulates the behemoths. Banks the size of Citibank are "too big to fail," and nearly every past business cycle the Federal Reserve has had to bail them out. Will monetary policy now be used to bolster bank earnings if insurance or stock problems threaten the health of Citigroup? We hope not. We also hope the Fed centralizes the supervision of these giants under its wing.

Oh, yes. Now that the real world has bypassed Congress once again, we expect the legislators to finally update the 1933 Glass-Steagall Act. Citigroup has just made it meaningless.

MICROSOFT: WHAT TO DO—AND NOT TO DO

What, if anything, should Washington do about Microsoft? There is no more important economic policy decision facing the U.S. today. Microsoft Corp. is at the heart of the high-tech New Economy. It is a driving force behind America's amazing prosperity. Yet that very centrality and power raise important questions that cannot be avoided. Anything the Justice Dept. suggests is risky. Amid rapid technological change, the law of unintended consequences is at full force. Smothering the nation's high-tech powerhouse with heavy-handed regulation is the worst possible outcome. But doing nothing may also be unacceptable. In the end, any policy decision must be measured by one economic standard—does it enhance competition and hence choice for consumers?

Microsoft's pervasive and growing presence is undeniable. Its Windows operating system dominates PCs with 90% of the market. Its NT software ran 40% of network servers sold last year. Its browser is heading toward a 50% share of the market. Its corporate Office software package has 95% of the market.

Certainly, there are economic benefits that accrue from that dominance. The Windows operating system standard makes possible a unified market for computers and applications software. Everything can be plugged in, integrated, and made to work. Microsoft is entitled to the benefits of that standard. But, unchecked, a monopoly can do serious harm.

Take pricing. In an industry characterized by falling prices, Microsoft is able to raise prices or avoid cutting them. Computer makers see that as monopoly power. With computer prices falling below \$1,000, computer makers are driving down prices charged by chipmakers and hard-drive producers. Only Microsoft has the market power to hold its price line.

Monopoly power also threatens competition. Before yielding to Justice pressure, Microsoft had exclusive contracts with PC makers to ship its browser, but not Netscape's, as a

condition of licensing the Windows operating system. It had contracts with 40 Internet service providers requiring them to promote its browser. Under government pressure, Microsoft backed off. Yet, with the new Windows 98, Microsoft again favors its own Web sites and those of its partners.

Leveraging monopoly control of computer operating systems into monopoly control over the Net is simply not acceptable. What should be done? *BUSINESS WEEK* has examined the options in depth (page 112). It is very tempting to simply do nothing. Technology, after all, is changing at a tremendous pace, opening up opportunities for new players. But many of these players complain of not being able to compete freely.

Then there is the extreme option of breaking Microsoft in two. A software applications company would compete with thousands of companies writing programs while the operating system would become like a common carrier. This would do the leverage Microsoft gets out of its monopoly but at a price of possibly destroying an engine of economic growth.

We favor a middle road. Call it regulation-lite. If Microsoft leverages its monopoly to squelch competition, its conduct should be checked quickly. For example, Justice should allow Win98 to have an integrated browser, as Microsoft wants, but insist on a version with a disabled browser so consumers can choose rival browsers if they wish—as is now the case with Win95. The government should clamp down on exclusive contracts that restrict competition. And PC makers should be allowed control over the initial desktop screen that pops up on their machines. Consumers would get better choices. At the same time, those choices should not be channeled.

How best to promote competition and innovation is a question with no simple answer. In the end, the markets will determine the fate of Microsoft. But corporate behavior that limits competition and choice must be checked.



UNLIMITED PARTNERSHIP
ROGER KECK OF PILGRIM'S PRIDE AND SCOTTY MARTIN OF ARAMARK

WE FOUND \$250,000 IN

savings and had an 11% drop in operating costs just by letting ARAMARK do

THE LAUNDRY.

"Our partnership began with ARAMARK providing us with maintenance uniforms, mats, and towels," says Roger Keck of Pilgrim's Pride. "So when Scotty Martin and his team from ARAMARK came to me about expanding to a smock rental program, I was interested to hear what he had to say. We've got 30,000 smocks that need to be washed every week, and the way our old washing machines always broke down, I never knew if we'd make it. And as you can imagine, the maintenance really got expensive." At ARAMARK we're always looking for new and innovative ways to make our partners' job easier. And at Pilgrim's Pride we knew a smock rental program would not only save time, but also money. We pick up and deliver every day. We even developed a system that lets workers select their size and color smocks a lot faster. Roger adds, "In the first year we saved \$250,000 and had an 11% cut in operating cost. Things are going so well we're bringing ARAMARK in at three of our other locations."

To learn more about Managed Services through Unlimited Partnership call 1-800-ARAMARK or visit us at www.aramark.com



Business Week

April 27, 1998

THE MCGRAW-HILL COMPANIES / \$3.95

TRILLION DOLLAR BANKS

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WHO
THEY'LL
BE

HOW
THEY'LL
WORK

CAN
THEY BE
REGULATED?

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HOW DECENT
PLASTIC SURGERY CAN MAKE
A PERSON YOUNG AGAIN.

WE'VE FIGURED OUT HOW TO DO IT
WITH OLD OIL FIELDS.





**HOW TEXACO'S RELENTLESS
PURSUIT OF ENERGY PUMPED NEW
LIFE INTO AN OLD FIELD.**

After 100 years, California's Kern River oil field needed a little help. Even though there was plenty of oil, there was no way to get all that oil out.

Then some of the bright young minds at Texaco came up with a new way to use a process called multi-zone steam flooding, and turned an old field into a veritable fountain of youth.

You see, the oil was hidden in layers of rock and sand. They forced steam into those layers and heated the oil, so it could separate from the earth and be pumped to the surface.

Suddenly, a source that was nearing the age of retirement is producing millions of new barrels of oil. And counting.

By rejuvenating oil fields at Kern River and elsewhere, we can now get astounding amounts of additional energy. All the tummy tucks and liposuction in the world couldn't work that kind of miracle.

It's all part of our relentless search for the energy to keep the world running. To learn more, pay us a visit at www.texaco.com.



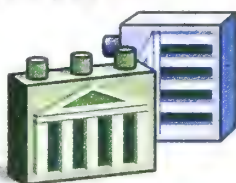
A WORLD OF ENERGY.™

COVER STORY

TRILLION-DOLLAR BANKS

Other huge mergers are sure to follow NationsBank-BofA. Will they pay off?

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BusinessWeek

APRIL 27, 1998



Cover Story

32 \$1,000,000,000,000 BANKS

Once, it was unimaginable. Now, after three eye-popping megamergers in eight days, it seems inevitable. But will ultra-big really be better—for bank customers, for the economy, or even for the banks themselves? The indigestion suffered by recent megamergers, the widening scope of rival financial-service vendors, and the rise of online commerce do not bode well

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Some expect lower costs from the megabanks, but others fear reduced competition

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Regulators are way behind the curve—and a pile of taxpayer money is at stake. Here's how the watchdogs can catch up

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But investors don't care. They're counting on a rebound in the second half

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Production glitches are costing the aerospace giant big time, and a post-merger culture clash isn't helping

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Love him or hate him, American's hard-charging CEO has left an indelible stamp on the airline industry

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A judge's ruling suggesting that the chipmaker is a monopoly could embolden rivals and the feds

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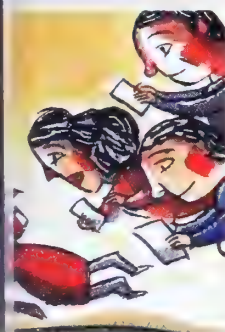
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A national organization hopes to gain AARP-type clout as it aims to mobilize moms and dads



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A new class of drugs promises to cut off
a tumor's blood supply—without the side
effects of chemotherapy or radiation
DEVELOPMENTS TO WATCH
Nanobots, light lithium batteries, folic
acid dosage, biological warfare fighters

Information Technology

TECHNOLOGY & YOU
A new clipboard saves handwritten
notes—and allows keyword searches
SECURING TRAFFIC ON THE NET
Companies battle each other to sell
services that let them monitor consumers'
online habits
TRACKING WHO SURFS WHERE
Companies struggle to pry more info
out of wary cybernauts

Media

THE TIME FOR PRIMESTAR?
The satellite broadcaster could soar if
the Justice Dept. finally clears its
long-delayed merger with News Corp.



HERE COMES THE EURO

The potential
benefits are
limitless—and
so are the risks
page 50



NOBODY DOESN'T KNOW SARA LEE

But brand recognition isn't enough, so it's
planning a leaner marketing machine page 114

CLICK CLIQUE

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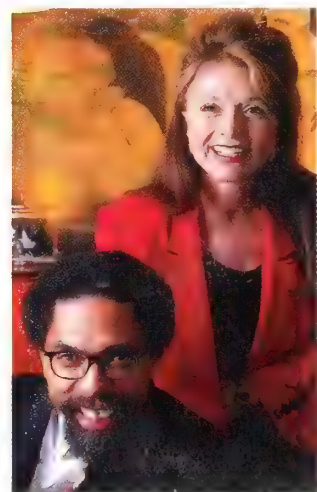
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A new group calls for
a bill of rights for
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TRUCK MANIA

Why so many U. S.
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Science & Technology

LIVING TUMORS TO DEATH
A new class of drugs promises to cut off
a tumor's blood supply—without the side
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long-delayed merger with News Corp.

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A revolution is at hand, and it will go
well beyond a new currency. Monetary
union will sweep away Europe's national
corporations, rigid work rules, and lush
pension payments. In their place will
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largest in the world

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EDITED BY ROBERT McNATT



STREET NEWS

HOW NOT TO EASE A MARKET CRASH

UH-OH. THERE COULD BE A problem brewing in the new circuit-breaker rules set for the financial markets. Regs just adopted by the New York Stock Exchange temporarily halt trading if prices fall 10%, and again at 20%, a drop of about 1,800 points in the current Dow Jones average. The old rule stopped trading with a drop of as little as 350 points.

The problem is over at the Chicago Mercantile Exchange, where futures contracts on the Standard & Poor's 500-stock index let traders hedge to cushion big swings in the stock market. Under the

THE MERC: Different regs

Merc's new rules, the price of the futures contract can't drop more than 20% for the whole day. So in a situation such as the 23% decline in the crash of October, 1987, stocks could be traded, but not futures contracts.

That, say traders, could make a bad situation worse. David Peterson, an institutional floor broker at the Merc for Sakura Dellsler, says that "clients could have a very serious problem with this." But he expects that the Securities & Exchange Commission and the Commodity Futures Trading Commission, which oversees the Chicago Merc, will see to it that the exchanges hash out their differences. *Andrew Osterland*

CHINA SYNDROME

APPLE DENIES AN AD'S PASSPORT

WILL 1.2 BILLION Chinese and other Asians recognize Amelia Earhart more readily than the Dalai Lama? Well, Apple Computer recently chose the American pilot instead of Tibet's Buddhist leader to portray in its "Think Different" ads for the Asia-Pacific region. Since China forced the Dalai Lama into exile in 1959 after it invaded Tibet, critics say Apple is playing politics.

Apple says not. "This campaign isn't about politics or creating controversy. It's about celebrating people who



THE DALAI LAMA

have done great things. Not everyone in China may feel that way about the Dalai Lama," says a spokeswoman. So the faces of Gandhi, Picasso, Einstein, Alfred Hitchcock, and Muhammad Ali will be used instead—along with Earhart. The Dalai Lama is being used in the U.S.

Dawa Tsering, the Dalai Lama's representative for the Americas, noted that across Asia "there are lots of Buddhists, and they know His Holiness very well." As to Apple's motivations, he said, "I think maybe from the Chinese side they are having some pressure." He added that he had no idea who Amelia Earhart was. *Joan Oleck*

TALK SHOW "It's a huge distraction, there's no two way about it."

—New York pitcher Dave Cone, after the collapse of a section of Yankee Stadium

RETAIL TALES

ARE DEBIT CARDS ROBBING STORES BLIND?

THE POTENTIAL COST OF A flap over credit- and debit-card processing fees just hit a cool \$1.9 billion. Several big retailers fighting Visa USA, MasterCard International, and the cards' 4,400 issuing banks, have asked a federal court in Brooklyn to make an ongoing antitrust case against the card issuers a class action. The merchants also say they are being overcharged by the card issuers, so they're asking for big money.

The stores initially contended that Visa and MasterCard force them to accept debit cards along with credit cards—an alleged violation of antitrust laws. Now, the retailers add that the card issuers price debit-card trans-

actions unconscionably high, up to \$1.38 to process a transaction that could be done for as little as 7¢.

Since the suit began about two years ago, Circuit City and The Limited, among others, have joined original plaintiffs Sears Roebuck and Wal-Mart. Damages sought

for the past five years would total at least \$1.9 billion, says attorney Lloyd Constantine. Originally, no dollar damages were specified. Patricia Allen, who represents Visa, says 14 million merchants sign up all its products

can still decline to accept debit cards as payment. A court may rule on the class action status as early as this summer. *Dennis Blum*



COSTLY to retailers

MAD AVE

SOUTH PARK'S CANNY BAIT-AND-SWITCH

ON APR. 1, COMEDY CENTRAL toyed with viewers of its raunchy hit cartoon show, *South Park*. That night, it had promised a long-awaited revelation: the paternity of Cartman, a spoiled little fat kid addicted to Cheesy Poofs. "April Fool!" said Comedy Central, which postponed the disclosure, angering thousands of the show's fans.

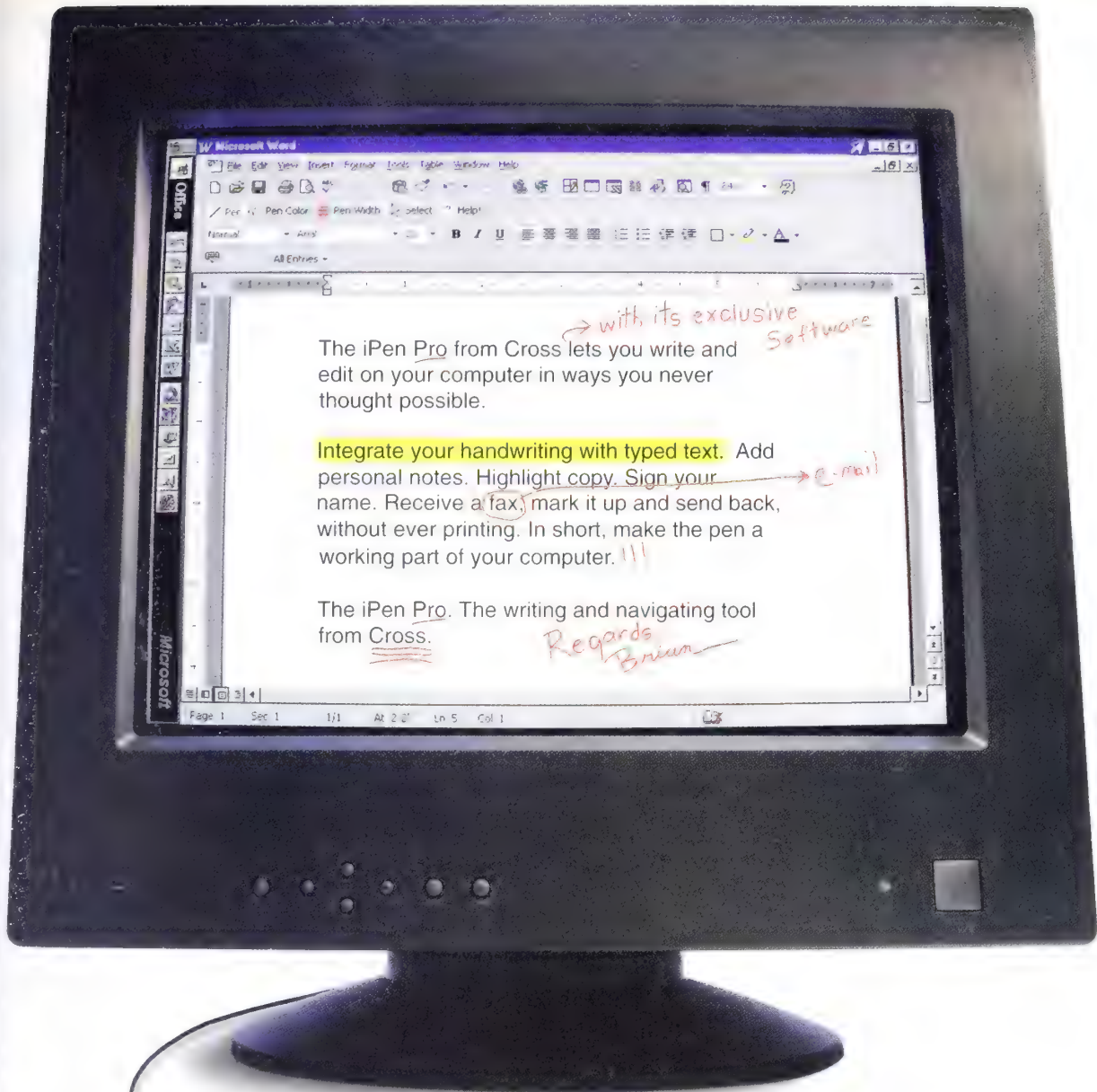
Viewers be damned: Ad-

vertisers are thrilled because the delay means that they be getting a bigger bang for their buck. Larry Divney, Comedy Central's vice-president of ad sales, says advertisers who a year ago bought 30-second slots, expecting a 0.9% share of the network's 43 million subscribers could now enjoy as much as a 1% share on Apr. 22, when Cartman's father is unmasked.

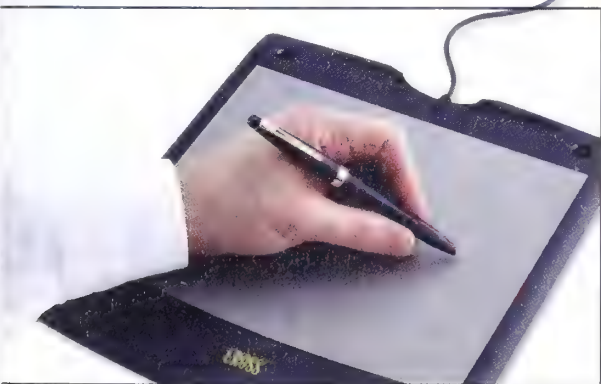
South Park is the highest rated nonsports show on cable TV, with ads selling an average of \$40,000 for 30 seconds. Last-minute buyers pay up to \$80,000. Anyway, did Comedy Central plan this way? "It was a fortunate circumstance," Divney says, looking to future ad revenue.

So is Cartman's dad Jesus, one of the '91 Denver Broncos, or who? Check out "Cartman's Mom Is Still a Dirty Slut" to find out. The plot sickens. *Joan Oleck*





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Up Front

CORPORATE CULTURE

SEE DICK RUN. SEE JANE ANALYZE DATA

ALTHOUGH COGNEX, WHICH makes machine-vision inspection systems, is a 17-year-old company, sometimes it acts like a little kid out to get attention.

On June 2, the company, which has annual sales of \$155 million, will host 50 financial analysts for an annual update. Nothing unusual about that, except that the meeting will be modeled after a day at an elementary school. A yellow school bus will shuttle attendees

from a swank Boston hotel to a confab complete with blackboards, lunch boxes, and a pop quiz. CEO Robert Shillman will dress as a school principal. But the analysts

won't have to ask permission to use the bathroom. "We'll try to make them as comfortable as possible," says a company spokesman.

What's the angle? Shillman

just likes to have fun. Last year, he handed out bonuses from the back of a Brinks truck. Analysts will focus on the numbers, which could suffer this year because of problems among computer-chip-making customers. Still, the wacky approach makes an

impression. "They did *Star Trek*," at last year's meeting, says Fred Wolf, an analyst at Adams, Harkness & Hill. "It will be a tough act to follow." *Paul Judge*



TEXT: Got crayons!



SLUGFEST

TAKE A SEAT, GUYS. NO, WAIT...

PAT RILEY AND HIS PLAYOFF-bound Miami Heat basketball team are taking a little heat of their own. The team has been accused of snatching 38 basketball-player-size leather seats from a plane it chartered from Pan American World Airways. Pan Am says that after it filed for Chapter 11 bankruptcy this year, the Heat moved in and took the seats. Creditors

estimate the seats are worth \$10,000 each.

What's worse, Pan Am says the Heat took carpeting, cabin dividers, and video equipment, too. Heat attorney Nick Christin says it was all gear the Heat owns under its charter agreement.

But creditors think they have a claim to the seats. They're calling foul. The removal, says Paul Singerman, a creditors attorney, violates a court order not to remove property from a debtor in Chapter 11 without court permission. The seatnapping was also carried out without the Federal Aviation Administration approval needed for aircraft alterations, he says. The Heat would not comment.

So has a law been violated? That's up to the bankruptcy court. The team won't say which airline it's flying these days. Meanwhile, its seats, sitting in a Miami warehouse, are missing the playoffs. *Dennis Blank*

DRAWN & QUARTERED

THE NEXT MEGAMERGER



PRODUCT PEEK

SMILE, YOU'RE ON CANDID GAME BOY

MOVE OVER SONY, CANON, AND Olympus. Companies such as these are trying to dominate Japan's budding digital camera market with ever-so-sophisticated models, but game giant Nintendo has stolen the show with its low-tech Game Boy Camera. In the first five weeks of the camera's sales (Feb. 21 through Mar. 31), Nintendo says it has sold more than 700,000 units of the \$50 lens and camera cartridge, which attaches to its handheld Game Boy machine. Last year, only 1 million digital cameras were



sold in all of Japan, which is half the world market.

Fans can store up to 100 black-and-white pictures on the microcamera and view them on the Game Boy screen or print them out on a \$60 printer manufactured by Nintendo by Seiko Epson Corp. The quality is grainy, but the Game Boy crowd, mostly ages 8 to

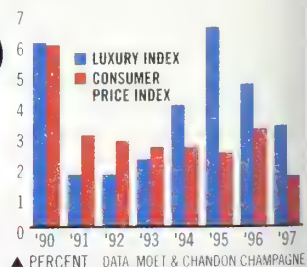
A SNAP: Nintendo

18, doesn't seem to mind. As with more sophisticated digital systems, they can stretch and split images or decorate them with special stamps and "paints." Nintendo, which assembles the camera at its Kyoto plant, is ramping up for a June 1 U.S. launch. *Irene M. Kwiat*

THE BIG PICTURE

WHY THEY CALL IT THE HIGH LIFE

Buyers of luxury goods and services aren't too cost-conscious yet while luxury prices continue to outpace general inflation the pace has slowed. A round trip on the Concorde has risen 18%, but at least Porsches and caviar still cost the same.



Credit-card users who canceled cards, 1997, 36%. Reasons: too many cards, 13%; no longer buying on credit, 7%

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I know which buttons

A woman with blonde hair, wearing a black blazer and sheer black stockings, is sitting on a dark wooden bench. She is looking directly at the camera with a slight smile. Her right hand is resting on the keyboard of a laptop that is open on the bench next to her. The laptop screen displays a web interface with various buttons and text. The background is a plain, light color.

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 **network**
ASSOCIATES
Who's watching your network

than eyes the Net," Government, 6). Nor will it stand idly by and let someone else threaten it. That's why Governor Pete Wilson is fighting within the National Governors Assn. in favor of Representative Christopher Cox's (R-Calif.) Internet-moratorium legislation. And why California's Board of Equalization explicitly rejected the notion of a company's presence on a Net [in California] subjects it to tax—contrary to what was stated in the article.

Aggressive tax schemes are a threat to providers of Net hardware, software, and services. They also can hurt businesses that compete better at lower costs by using this technology, as well as individuals who use the Net to work, communicate, and learn.

Ira H. Goldman
Electronic Commerce Advisory Council
Sacramento

PEOPLE A DAY KILLS THE MICROBES AWAY?

Bacteria and viruses reproduce faster than we ever will and, as a consequence, will always be an evolutionary step ahead of a pharmaceutical strategy "against the microbes," Cover Story (p. 6). Antibiotics, vaccines, and drugs certainly have a place in fighting infections, but we must remember that no drug can make up for a weak immune system.

Garbage, pesticides, and a host of other things we ingest—including some antibiotics—actually reduce our ability to fight infections. So do nutritional deficiencies, which are more common in the U.S. than a lot of officials would like to admit. To shore up our innate defenses, we must also value scientific soundness, low-tech, low-cost weapons: eating wholesome foods and taking vitamins E and C to enhance our immunity.

Jack Challem
Editor and Publisher
The Nutrition Reporter
Beaverton, Ore.

LET THE CABLE COMPANIES KEEP HOLD

Today, having cable companies own and manage the wire into my house is as absurd as being the conduit for all programming is like having a trucking company own all the roads to individual homes ("Clipping cable's power," News Analysis & Commentary, Apr. 6). They are, consequently, filled with a concentration of monopolistic power regardless of regulatory oversight and choose to exploit and deliver whatever they wish.

I would urge Congress to separate the "ownership" of the cables and the "retailing" of the programming. If companies were allowed to bid for the servicing of the physical infrastructure separately, consumers would get the benefit of dozens, if not hundreds, of "programming retailers."

The company responsible for servicing the infrastructure would have no preference for any one retailer. Their services would be paid for by the fixed charges for the line that regulators

would allow them to charge (much like the line charge on my phone line). This arrangement would also make it possible for program creators to offer à la carte channels directly to consumers, further reducing their costs by taking out the middleman.

Everyone would gain: consumers, because they would have a choice of retailer; retailers, because they would have a selling opportunity; creators, because they would be able to offer service directly to the consumer; and gov-

WillTales



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the E 430's all-new, twin-spark V-8 that can go from 0 to

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than the mother of streaking, Lady Godiva.) With a

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ernment, because it would have less to regulate.

Arshad Noor
Cupertino, Calif.

The most obvious reason for the price rises: Cable companies fear reregulation and are jacking prices as far as they can to have a higher base from which to be regulated. It's a defensive strategy—for which all consumers will suffer. This is corporate spin reminiscent of tobacco presidents on cancer risk—not the best model with which to win the hearts and minds of either consumers or the government.

David Wineberg
Internet Tradeline Inc.
New York

FOUL RESULT OF THE WASTE MANAGEMENT MERGER

Regarding your question, "Can Waste Management climb out of the muck?" (News: Analysis & Commentary, Mar. 23), Ecology Group works with trash-removal vendors. To create profits quickly, the "new" Waste Management Inc. will increase prices across the board to all of its current clients. It will acquire smaller hauling companies or force them out of the market—or both. If the latter occurs, competitiveness in this market will be dramatically reduced, and businesses will find more of their money going into the trash.

Before this merger, the businesses we have worked with typically saw annual price increases of at least 15%. With less available competition, and with John E. Drury's aggressive profitability goals, these increases will become more commonplace. The people who will be hurt are managers for retail chains, quick-service food purveyors, casual dining chains, drugstore and grocery chains, etc., which are often responsible for controlling expenses at their sites. It can mean the difference between a bonus or no bonus for them.

Renée K. Nicholson
Ecology Group
Columbus, Ohio

PRIVATIZING SOCIAL SECURITY: WHAT ABOUT THE MENTALLY ILL?

Doubts about the privatization of Social Security go beyond yields on stocks and income for the physically disabled and dependents of deceased workers ("How to fix Social Security," Economic Trends, Mar. 23). A more compelling reason to reject privatization proposals is that they decimate the dis-

ability-income and survivor-insurance payments that provide a floor of protection for those most in need—those with mental retardation and other disabilities. We must not let that happen.

Quincy Abbot
Arlington, Tex.

BUSINESSES SHOULDN'T BE SO QUICK TO EMBRACE ARBITRATION

Many employers seem entranced by the idea of saving costs through mandating arbitration in employment contracts, as your story points out ("Forced into arbitration? Not anymore," Legal Affairs, Mar. 16). They should consider, however, that arbitration clauses make it easier, cheaper, and faster for employees to file claims against them, too.

Employers should be wary of agreeing so easily to arbitration for disputes arising out of the employment relationship. It can be a double-edged sword, particularly for smaller businesses.

J. D. Thorne
Crivello Carlson
Mentkowski & Steeves
Milwaukee

HAVE NO FEAR: THE GODZILLA CAMPAIGN IS A MONSTER

Stop gnashing your teeth ("He's big. He's upset. He's invisible," Marketing, Apr. 6). So what if the marketing campaign of the filmmakers and Sony Corp. isn't traditional? Formula marketing isn't necessary when you have a property with 40-plus years of equity and the highest consumer-awareness level possible. The teaser campaign is working. It was controversial enough for BUSINESS WEEK to write about it. With two more films waiting in the wings, this licensee thinks the long-term marketing approach is a well-conceived monster.

Leo Hauser
Co-CEO
Trendmasters Inc.
St. Louis

WHY MATURE COMPANIES RARELY MAKE BREAKTHROUGHS

"The new trailblazers," (Special Report, Apr. 6) chastises the leaders of established phone companies and applauds new-technology mavens. But you miss a fundamental point: Rapid, dramatic technology advances and their associated cost reductions fly in the face of the "entitlement" mentality of investors and analysts who influence decisions by corporate leaders.

Imagine what would happen if the

CEOs of AT&T or Ameritech Corp. acted on the reality that new converged-voice data technology is better and cheaper than the installed plant. Billions in assets would be written down, and prices for existing services would be cut 50% or more. As current prices, margins, and earnings fell apart, investors would be sorely disappointed.

Clearly, the ability to move from one generation of technology to the next favors new providers. They need not eat much, if anything, while they build out the new infrastructure and build up new business by cutting existing prices.

Such transitions present one of the great leadership issues of our time. Unless a business dominates a horizontal layer of high tech (as Intel and Microsoft), it's tough for a market leader in one generation to succeed in the next.

Dennis J. Cray
Prospect, Ill.

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WASSERSTEIN'S
&A 101

The rehabilitation of Bruce Wasserstein has not been quick or easy. The mergers-and-acquisitions maven hit his nadir in 1989, he landed on the cover of *Forbes* with the headline "Bid-'em-up Bruce." The perception of Wasserstein as an aggressive investment banker who won hostile bidding wars by getting clients to overpay faded with time. He has kept a low profile during this decade.

February of 1997, however, he shed the spotlight again when he was named as adviser to Dean Witter Discovery & Co. in its merger with Mortenson & Co. In early 1998, his firm, Wasserstein, Perella & Co., celebrated its 10th anniversary with full-page newspaper ads. Some 500 employees, the firm has made a name as a top M&A adviser that has prospered during the merger boom of the 1990s.

Wasserstein may have written *Big Deal: The Battle for Control of America's Leading Corporations* to help companies achieve public redemption. The 50-year-old New Yorker says he wrote the book because "it was in me." The book may have been in him, but his inner editor was on vacation. The 820-page tome, however, has an underlying thesis: that mergers and acquisitions, while good for the economy, are difficult to do. Here's welcome relief in the form of chapter-opening quotes and profiles on such subjects as Viacom, Sumner M. Redstone and buyout of Henry R. Kravis. And the last is a thorough primer on the nuts and bolts of tender offers and bear hugs, and attempts to pressure companies into deals. But much of the book is an inspired rehash of recent deal history, including chapters on specific industries from energy to health care.

Deal is certainly not "highly readable and more compelling than *Barbarians at the Gate*," as its book-jacket

copy says. Wasserstein's sister, playwright Wendy, is the writer in the family. Bruce's prose is workmanlike and emotionless, betraying his first career as a lawyer. Nor does he dish any dirt on his famous clients and fellow bankers. Wasserstein ignores the first rule of writing, which is show, don't tell. And for gosh sake, name names! For example, in describing negotiations, he says, "there is the occasional pathological bully. Some people just can't help themselves and rant and rave with red-faced demonstrations of temper." Hmm. Or how about this wonderfully cryptic sentence: "Being the subject of press scrutiny is a rather remarkable experience, even for someone sympathetic to journalists." Indeed, the only emotion to surface in the book is the author's fear of reporters.

Why is Wasserstein so unwilling to share his undoubtedly rich cache of experiences? Because he is a working investment banker who very much wants to eat lunch in this town again. He has a business to run and can't afford to alienate his clients. The talented journalists who wrote *Barbarians at the Gate* had far less to lose.

One of Wasserstein's main motives appears to be defending his profession and himself. In response to charges that deals were overpriced in the 1980s, he points out that, in hindsight, the critics were wrong. He rebuts the criticisms of mergers, with his best counterargument being that they allow companies, and thus the economy, to compete and prosper. His analysis of the merger boom is thin: Wasserstein chalks it up to factors from regulatory reform to technological change—nothing we haven't heard before.

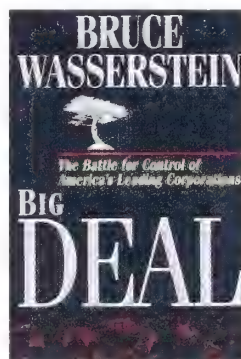
Yet *Big Deal* shines in its final third, the section called "Doing the Deal." Here, Wasserstein's keen instincts, knowledge of legal and accounting issues, and gamesmanship abilities are apparent. Ironically, one of Bid-'em-up Bruce's best chapters is "The Price," which discusses in detail how to value a company.

Another good chapter gives advice on negotiating tactics. "One ideal way in which to control pace is to be the host for the meeting," we are told. Wasserstein also advises that "all anger need not be repressed.... A show of anger may well be justified by the situation, particularly if you feel the other side has begun to try to take advantage of your flexibility." Or how about this: "Sometimes there is great advantage to confusion." *Big Deal* also details the mechanics of dealmaking, from defense tactics to raising cash. "The most common mistake sellers make in negotiated transactions is granting a prospective buyer the exclusive right to negotiate a purchase for a period of time." For certain readers, this advice could be well worth the book's \$30 price.

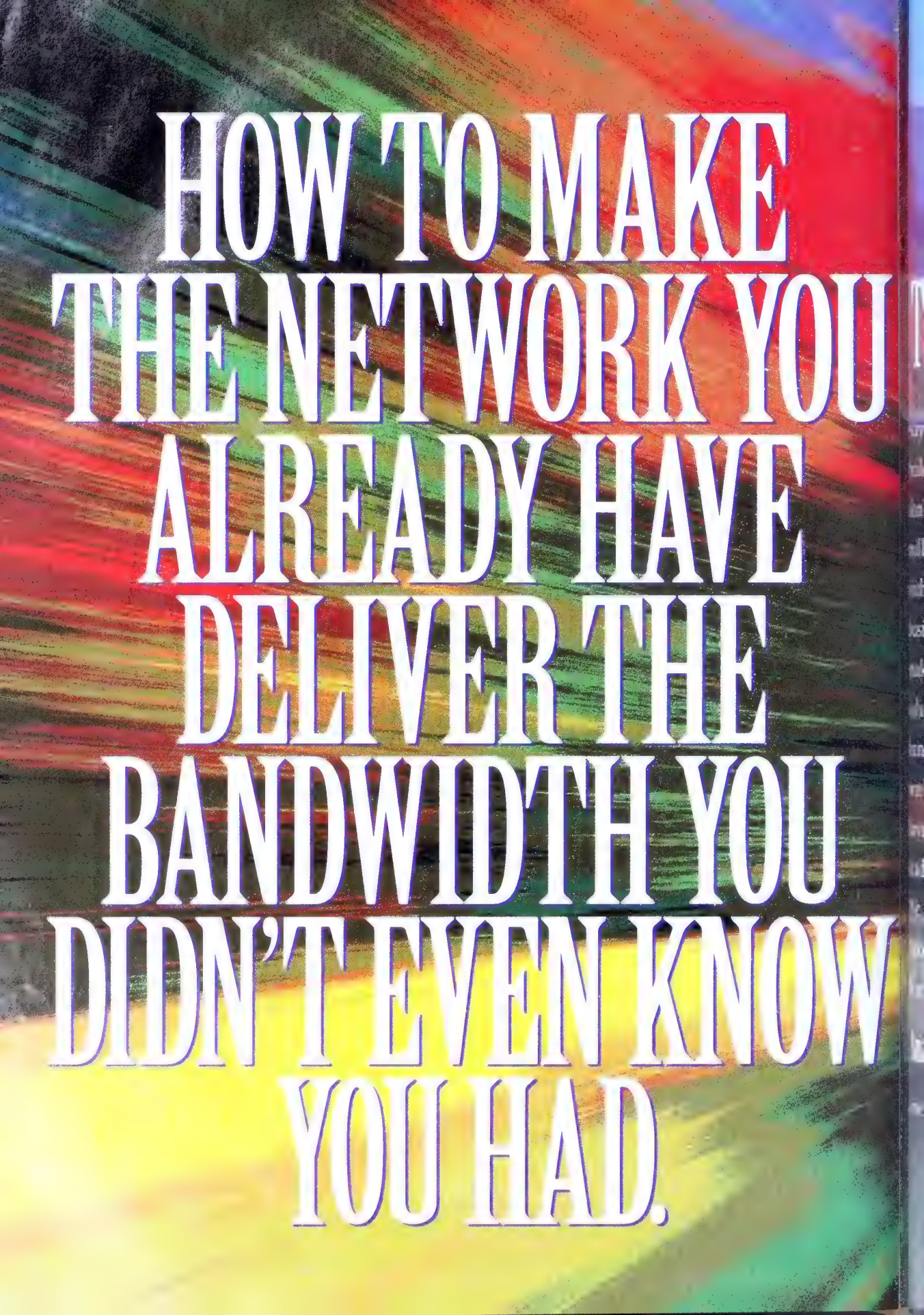
Wasserstein performs a service by stripping away some of the mystique surrounding what highly paid investment bankers actually do, such as run auctions. However, he is largely uncritical of his profession. The only time he acknowledges potential conflicts of interest is in a discussion of "fairness opinions"—when a board of directors hires an investment bank to give its opinion on whether shareholders are getting a fair price. Wasserstein points out that investment banks receive a success fee if the deal they are advising on goes through and get a much lower fee if the deal collapses. It would be nice if he had pointed out other such conflicts.

Wasserstein has written a solid textbook that will be a very useful reference for directors, managers, aspiring investment bankers, and journalists. It is hardly a page-turner. But it may impress a few clients and even get people to replace his hated nickname, Bid-'em-up Bruce, with another: Big Deal Bruce.

BY LEAH NATHANS SPIRO
Spiro covers investment banking.



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BY STEPHEN H. WILDSTROM

A CLIPBOARD WITH A MEMORY

The CrossPad stores pages of handwritten notes—and allows keyword searches

For far too long, computers have forced human beings to do things their way. Humans have been communicating through speech since the origin of the species and by handwriting for thousands of years. Typing and mouse clicks, efficient though they may be, are unnatural newcomers.

The \$399 CrossPad from penmaker A.T. Cross is a sign that computers may be starting to do things our way. It's a sort of electronic clipboard; slip in a pad, pick up the special pen supplied with the device, and you can store up to 50 handwritten pages in the CrossPad's memory. Connect the clipboard to the serial port on a Windows 95 PC, and a facsimile of the handwritten pages is zapped into the PC.

You could accomplish the same thing just by running your written pages through a scanner. But the CrossPad, developed in conjunction with IBM's Thomas J. Watson Research Center in Yorktown Heights, N.Y., is more convenient and comes with some very clever IBM software.

INDEXED COPIES. If you tap a button on the CrossPad and then circle a word or phrase on your sheet of paper, it will be converted to text and recognized as a keyword when you copy the writing to your PC. After correcting the software's translation of your

handwriting, if necessary, you can search your saved notes for the reference. You can also add keywords to pages once they have been loaded into the computer. This makes it simple to store indexed, searchable copies of handwritten documents on your computer.

The IBM re-

in training the device to read my scrawl, it did a far from perfect, but still creditable, job if I wrote carefully. I certainly could fix the errors a lot faster than I could type in all the text, a reasonable measure of success.

Still, I think of the CrossPad mainly as a very interesting first effort. The clipboard is bulky and heavy, although researchers hope to design a version that is no thicker, and not much heavier, than a conventional clipboard. You have to click a button when you move to a new

sheet of paper, or your writing gets all jumbled. That's an inconvenience until you get used to it. And when you choose to recognize hand-

powered by an AAAA battery. That doesn't leave much room for ink, so Cross uses mini ballpoint refill good for roughly 50 sheets. Sets of refills are stored neatly beside the pad. But I'm not a fan of ballpoints and would like a rollerball or ceramic tip alternative. Many buyers might prefer something lighter than the 1.5-ounce model. And don't lose the pen. The first replacement costs \$59 and subsequent ones \$89.

Improvements—and lower prices—will come in time. In the meantime, the CrossPad is an important sign of things to come, as computer scientists make rapid progress on what they call "alternative interfaces" such as speech and handwriting.

At high-tech meetings, it's not unusual to see everyone around a conference table tapping away on his or her own laptop computer. But in most settings, such behavior is thought of as somewhere between weird and rude. In Europe and Asia, it's generally regarded as completely unacceptable. And the use of laptops is flatly prohibited in some places, such as courtrooms.

Furthermore, computer keyboards aren't great for note-taking. It's difficult or impossible to type diagrams, flowcharts, graphs, or equations into a computer. Software will make it possible to use the CrossPad to fill in printed forms, an approach that may help health-care workers and others who spend much of their working lives filling in forms. They may find simpler and more natural than a laptop or handheld computer.

Keyboards and mice will disappear anytime soon, all maybe never. But it's good to see that computers are starting to accommodate human forms of communication.

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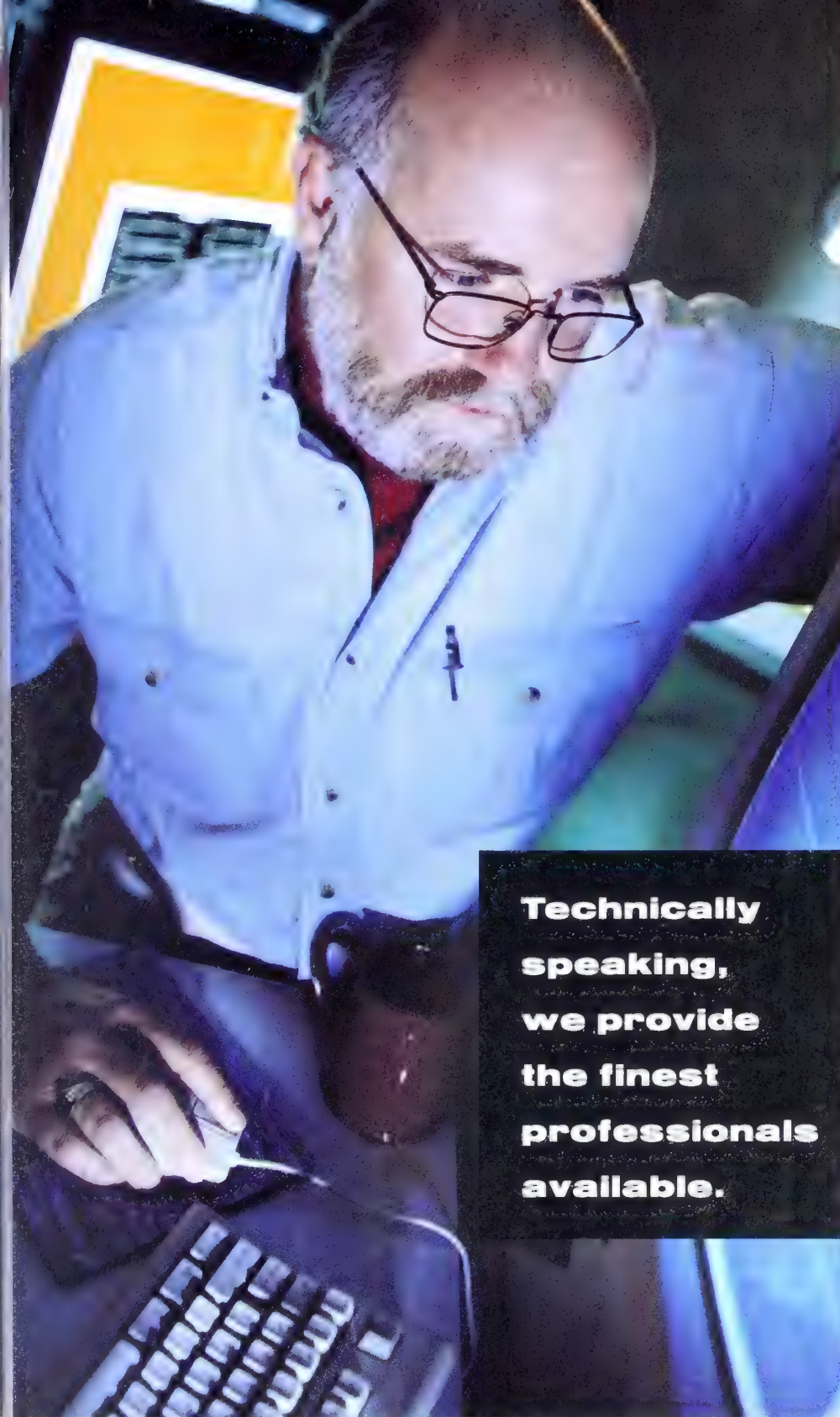
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approx. 50 pages

search team, headed by Krishna S. Nathan, is making only minimal claims for the CrossPad's ability to recognize handwriting. They want to avoid the ridicule heaped on Apple Computer's now-defunct Newton when it failed to come close to its early promise of handwriting recognition. But the developers may be selling their work short. The CrossPad can convert any selected block of writing to computer text. After investing 45 minutes or so

writing, the results show up only in IBM's Ink Manager program; to get the text into a word processor or other application, you have to cut and paste.

Oddly, given Cross's expertise, the pen could stand some work. The CrossPad uses radio signals from the pen to record data—that's how you can write through a whole pad of paper—so the pen contains a transmitter



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Expanding Possibilities

BY ROBERT J. BARRO

THE EAST ASIAN TIGERS HAVE PLENTY TO ROAR ABOUT



FLAWED:
Earlier studies suggested that the region's growth came mainly from a capital surge. Technology had a lot to do with it, too

Until last year, many East Asian countries were widely regarded as economic miracles. The standouts included the four Asian Tigers—Hong Kong, Singapore, South Korea, and Taiwan—where growth rates of real per capita gross domestic product from 1960 to 1995 were around 6% per year. Right behind were Indonesia, Malaysia, Thailand, and China. These performances placed this East Asian group at the top of the world's growth list.

The Asian reputation has suffered recently because of financial crises and recessions. These crises did highlight some policy shortcomings, such as unwise credit subsidies and deficient regulation of financial markets. But the negative reaction has been sharply overdone. In comparison with typical developing countries, government policies in most of the East Asian countries have been fiscally responsible, pro-market, and, hence, reasonable.

Yet even before the recent setbacks, the four Tigers' economic record was challenged in two well-known studies by Alwyn Young (in the 1992 *NBER Macroeconomic Annual* and the 1995 *Quarterly Journal of Economics*). Young argued that the high rates of economic growth reflected very little technological progress. Growth occurred mainly because of extraordinary rates of capital accumulation, some in the form of education ("human capital"), but most in machines and buildings. The lack of technological progress was surprising because, even if these countries were inventing little, they should have been benefiting from the superior techniques they were imitating from the world's most advanced countries. Historically, long-term economic growth has been sustained by significant increases in productivity due to technological and organizational change. The accumulation of huge amounts of capital and labor can work for a time, but ultimately must be backed by improvements in technology.

In Singapore, Young's analysis suggests that rapid growth was supported almost entirely by physical and human capital accumulation. In fact, investment was so high that the rate of measured productivity growth was actually negative. To Young, the high rate of investment persisted only because of the government's policies of forced saving and implicit subsidies to foreign capital.

The Young thesis was popularized and misinterpreted by economic journalists who even

compared some Asian economic policies to the high-investment programs of Stalin's Soviet Union. This argument never made sense, because the Soviet Union's output was valued at artificial prices made up by government bureaucrats. When realistic prices were applied in the post-communist '90s, the measured level of per capita output turned out to be low. In contrast, for the Tigers, most output is valued at world market prices, and there is no reason to think that growths are overstated.

SINGAPORE SWING. A recent study by Chai-Tai Hsieh published by the University of California at Berkeley challenges key parts of Young's conclusions on productivity growth. The most dramatic revisions apply to Singapore, where Hsieh notes that observed rates of return on investment have been roughly stable since the mid-1970s, not declining as Young's calculations would imply. Combine that fact with Singapore's robust growth in real wages, and Hsieh shows that measured productivity growth had to be positive—estimated 2.2% per year—rather than the -0.7% reported by Young. According to Hsieh, Young's analysis went wrong because of its reliance on Singapore's government national account statistics, which dramatically overstated the growth of the capital stock. Hsieh also found that Taiwan's productivity growth was better than previously assessed by Young (3.7% vs. 2.1%), but got less dramatic results for South Korea (1.5% vs. 1.7%) and Hong Kong (2.7% vs. 2.3%).

Even these higher estimates on productivity growth for Singapore and Taiwan underestimate the contribution of technological progress to economic growth. Improvements in technology raise the demand for physical capital (machines and buildings) and human capital (highly educated workers). But the resulting expansions of capital input are entered out in the usual calculations of productivity growth. A full explanation of the countries' growth would attribute more to the contribution of technology than Young's original thesis. It is improvements in technology that explain why so much capital accumulation could have occurred, especially in Singapore, without encountering diminishing returns. Thus, overall, we continue to have ample grounds to view the East Asian growth and technological performances as miraculous.

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BY MIKE McNAMEE

WILL ASIAN WOES TAR U.S. PROFITS?

Not likely. But exports may suffer

Six months into the Asian crisis, economists are still debating how the financial meltdown will affect growth in the U.S. Two new studies present a mixed picture: While the collapse of Asian currencies may have a larger-than-expected impact on American exports, profits of U.S. companies could weather the storm. The reason? Foreign subsidiaries of U.S. multinationals make the lion's share of their sales in Europe, not Asia.

Exports' vulnerability emerges in a study done by Andrew B. Bernard of Yale University and J. Bradford Jensen of Carnegie Mellon University of America's recent export boom. From 1987 to 1994, inflation-adjusted U.S. exports grew at 8.2% a year. That surge, coming as American manufacturers streamlined and cut costs, has powered a wave of optimism about U.S. productivity and competitiveness.

But the export boom was not mainly driven by greater competitiveness, Bernard and Jensen conclude. Using plant-level data, they find that rising productivity at U.S. factories accounts for only 10% of the increase in exports. Instead, the dollar's late-1980s depreciation and strong income growth overseas "were the dominant source of the export boom." With the dollar now gaining strength—and Asian consumers on the ropes—their results suggest that U.S. exports could be hit harder than many forecasters anticipate.

Falling exports, however, may not drive down U.S. profits. Economist

Joseph P. Quinlan of Morgan Stanley Dean Witter & Co. notes that exports account for only 24% of overseas sales by American multinationals. Those companies sell three times as much through overseas affiliates. And Europe accounts for a whopping 58% of such foreign-country sales

WHY EUROPE IS STILL IMPORTANT

SHARE OF SALES BY FOREIGN AFFILIATES OF U.S. MULTINATIONALS*



by U.S. affiliates, vs. just 8% for Japan and 8% for Southeast Asia. With Europe poised for an investment-led upswing, "a number of American companies are positioned to escape the pain of Asia via greater sales growth in Europe," Quinlan says.

A CASE FOR CUTTING PORK

States keep a sharper eye on costs

Budget hawks on Capitol Hill are trying—with little success—to block a \$217 billion highway-and-transit bill. For example, House Budget Committee Chairman John R. Kasich (R-Ohio) would even cut the federal gas tax and let states raise their own levies to fund roads, arguing that this would force states to focus on the best projects.

A new paper from the National Bureau of Economic Research suggests Kasich is on the right track. Alison F. DelRossi of the University of Wyoming and Robert P. Inman of the University of Pennsylvania studied a 1986 law that forced local governments to pay for a larger share of big water projects such as shipping channels and shoreline protection. The result: Overall spending fell 35%, and the federal outlay dropped 48%. DelRossi and Inman suggest that the shift results from "a more efficient balancing of budgetary costs and benefits." Translation: The pork disappears, and only the good stuff remains.

HIGH SCHOOL GREENSPANS

How kids would handle Fed policy

It won't replace varsity football anytime soon. But a growing number of high school students are participating in an annual competition, started in 1995, to see who can propose the best monetary policy. This year the "Fed Challenge"—sponsored by the Federal Reserve Board and Citibank—drew entries from 208 schools. The five members of the winning team will each collect a \$10,000 scholarship, while their school receives a \$50,000 grant to establish an "economics laboratory."

Each team must recommend whether the Fed ought to raise interest rates, cut them, or stand pat. Federal Reserve Board Vice-Chair Alice M. Rivlin and two of her colleagues will judge the

May 4 national finals, which will require teams to make presentations modeled on meetings of the policy-making Federal Open Market Committee.

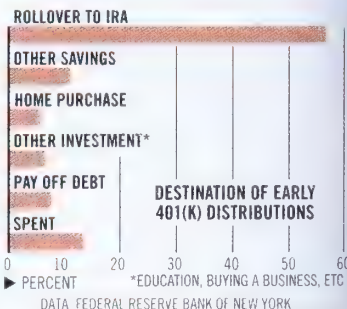
Some schools take it seriously. For example, last year's national champion Bryan (Tex.) High School—one of the finalists again this year—draws support from a schoolwide effort: Trained by their economics teacher, team members get coaching from the drama department and design help for their slides from art and computer students. The team even gets a pep rally as it heads for Washington. Can letter sweaters and economics students be far behind?

THE FLAW IN PRIVATE SAVINGS

Early withdrawals shrink 401(k)s

Last year's tax bill was supposed to encourage retirement savings by creating a new form of individual retirement account and new small-business pension plans. But at the same time, legislation has made it easier to tap into

CASHING OUT EARLY



those accounts before retirement for home purchases, college expenses, and other purposes.

New data published by the Federal Reserve Bank of New York may give Congress reason to rethink those early withdrawal policies. Among workers with 401(k) retirement plans, nearly half report having taken a lump-sum distribution before retirement—and almost half of that is spent or invested outside retirement accounts. Low-income workers are less likely to hang on to their savings until retirement: Among workers earning less than \$15,000, only 31% of pre-retirement distributions were rolled over into other retirement accounts. That's why some pension advocates warn that without strict limits on pre-retirement use of such accounts, low-income retirees could end up with few resources and no safety net.

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CANNING THE SKIES OR SIGNS OF SLOWER GROWTH

Will a red-hot economy spoil this low-inflation paradise?

U.S. ECONOMY The spring months will be critical for the U.S. economy. In the last quarter's surprising burst of spending, especially by consumers, both Wall Street and some Federal Reserve officials are starting to get a little antsy, fearing that inflation will remain benign. March reports on retail sales and job growth suggest that activity is throttling down from its breakneck pace. But so far, it's still hard to tell whether the cooling data presage a lasting shift to slower growth. It might be only the reverse side of the weather-related vigor in January and February—and the sizzling underlying trend may still be in place.

THE LARGEST RETAIL GAIN IN 11½ YEARS



QUARTERLY PERCENT CHANGE
AT ANNUAL RATES
DATA: COMMERCE DEPT., BUSINESS WEEK

But the first-quarter results were so strong that second-quartering may have to ease considerably to convince the financial markets and policymakers that any slowdown is real and lasting.

The economy's pace is especially important now, because much of the current strength is in services, where pricing power is less constrained by the Asian crisis and by global competition generally. One trend in the poor first-quarter profit results is that service businesses tended to fare better than goods producers. In March, price indexes were as tame as ever, but in labor markets in services historically tight, and with service wages accelerating, service prices are the place to watch for any nascent inflation pressures.

SELLERS OF RETAIL GOODS can only wish they had more pricing power, but for now, they are making the most of it in the sheer volume of goods sold. Retail receipts declined 0.1% in March, probably reflecting both the weather effect and a late Easter. Excluding car sales, sales rose 0.1%. Since receipts jumped 1% in January and 0.7% in February, sales for the quarter in-

creased at a 6.9% annual rate. But because of falling retail prices, primarily for gasoline and computers, real sales posted a 9.9% annual rate of increase, the best quarterly showing in more than a decade.

More important, after the retail data are adjusted to match up with the Commerce Dept.'s measure of consumer spending in the gross domestic product figures, BUSINESS WEEK estimates that real consumer spending on goods and services in the first quarter rose at an annual rate of about 6%. That would be the best quarterly performance in six years, and it would cap the strongest three-quarter run of consumer spending since 1986.

That exceptional showing means that consumer spending and housing outlays, which also shot up last quarter, will provide a powerful offset to the expected sharp widening in the trade deficit. As a result, first-quarter GDP growth, due out on Apr. 30, should easily top 3%, and some analysts expect growth of 3.5% or greater.

That's especially likely, since inventory growth appears not to have slowed as much as expected (chart). Business inventories in February jumped 0.6%, and first-quarter stock levels are rising as fast as they did in the fourth quarter. Even with the Asia crisis providing a sizable hit, the economy continued to grow in excess of the 2¼% to 2½% pace that most economists feel is consistent with keeping inflation down.

The weather effect was clear in the retail sales numbers. Sales at building-materials and hardware stores fell 0.6% in March, after posting huge increases of 1.7% in February and 3.8% in January. Department stores showed a similar pattern, with March sales off 0.2%, while buying in the two previous months increased 1.5% and 1.8%. April sales may rebound, given the stronger tone of the weekly retail surveys during the first half of the month.

INVENTORY GROWTH CATCHES UP WITH SALES



THE WHEN AND IF of slower growth will go far in setting the inflation outlook. Right now, the latest price data show no inflation problems, although the best news on the service side may be behind us.

Consumer prices for all goods and services were unchanged in March. Excluding food and energy, core

prices inched up a puny 0.1%. Over the past 12 months, total prices advanced 1.4%, as the 8.6% plunge in energy costs has offset other price increases. Core consumer prices, which exclude food and energy, are up 2.1% for the year.

But there's a divergence: Core service prices were up 3% in the year ended in March, while goods prices had hardly budged (chart). Service inflation in the first quarter was up slightly from the second half of 1997. That uptick shows how strong demand may be working its way into the inflation equation. The robust housing market is boosting the cost of shelter, which plays a dominant role in the consumer price index, while the tight labor markets are causing service wages to rise. In response, some service providers are trying to lift prices to cover their extra costs.

For example, when General Electric Co. reported a solid 13% gain in its first-quarter earnings, analysts noted that GE's service businesses generated the lion's share of revenues, amid a dearth of pricing power in the markets for the goods that GE makes.

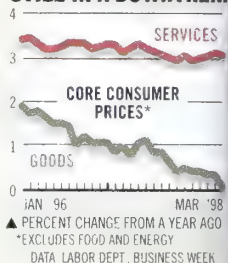
THE SITUATION IN GOODS PRODUCTION is different from services for two reasons. One, productivity gains are higher in manufacturing, so factories are covering their bigger labor bills by producing more during each work hour. And foreign competition is preventing some domestic businesses from raising prices.

Indeed, import prices continued their tailspin in March. But even in trade, not all pricing trends are alike. The biggest decline has been in commodities, mostly oil, but also metals and wood. The drop in raw material prices is the result of weak demand in Asia.

Prices of imported consumer goods are also falling, but the deflation rate has stabilized at 1% for the past half-year. The biggest surprise may be prices of imported cars, up 0.7% in March from a year ago. The gain suggests that some foreign carmakers, most likely those in Japan, are raising prices to earn more U.S. dollars. Over the past year, total nonoil import prices are down 3.2%.

But how much longer can this inflation paradise last in an economy that continues to grow in excess of 3%? That was on the mind of Fed Governor Laurence Meyer when he spoke on Apr. 9. Meyer warned that the economy's current pace was incompatible with keeping inflation down, and slower growth is required, preferably soon. Meyer saw only two ways to reach slowdown. "Asia may accomplish this," he said, "in which case it would substitute for monetary tightening that in my judgment would otherwise be required."

GOODS INFLATION IS STILL IN A DOWNTREND



MEXICO

CLAMPING DOWN TO BOLSTER CONFIDENCE

Working in tandem, Mexico's fiscal and monetary decision-makers are tightening policies to head off financial doubts caused by a weakening peso, low oil prices, and higher inflation.

Private economists and the Organization for Economic Cooperation & Development already expect Mexico's economy to grow between 4.5% and 5% this year—down from 7% in 1997—and several factors are worth watching. First, the collapse of oil prices has cut exports and public revenues—since the petroleum industry is a state monopoly. Oil sales account for 40% of government receipts. So the government has had to cut its spending programs

so far this year, for a total reduction of \$3 billion. In the meantime, the peso has weakened against the U.S. dollar, losing 6.8% from Jan. 1 to Mar. 10. The slide was stopped when the Banco de México removed some liquidity from the banking system, in effect hiking interest rates. The peso has regained 2.1% since then.

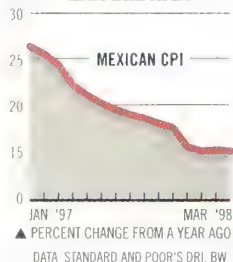
The weaker peso, coupled with strong domestic demand, is worsening Mexico's trade position. The trade balance in February posted a deficit of \$635 million, compared with a surplus of \$380 million a year ago. Exports rose a respectable 10.5% from a year ago, but imports surged 24.2%. The

trade balance is likely to end 1998 firmly in the red, after a surplus of \$600 million in 1997.

The peso-demand mix may also have stopped the rapid decline in inflation. Consumer prices rose 15.3% in the year ended in March, the same pace as in the previous two months (chart). If, in fact, the disinflation era is over, then Mexico's inflation rate will be higher than the government's 12% target for 1998 and higher than its 7% pace before the 1994 devaluation. That will put more downward pressure on the peso.

The twin restrictive stances could cause some rethinking about growth prospects, if not for 1998, then for 1999. But consumer spending, bolstered by rising real wages, and business investment still look strong enough for Mexico to avoid any serious slowdown.

IS THE DISINFLATION ERA ENDING?





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"HIGHEST IN CUSTOMER SATISFACTION," COMPUTERWORLD BUYERS GUIDE SURVEY

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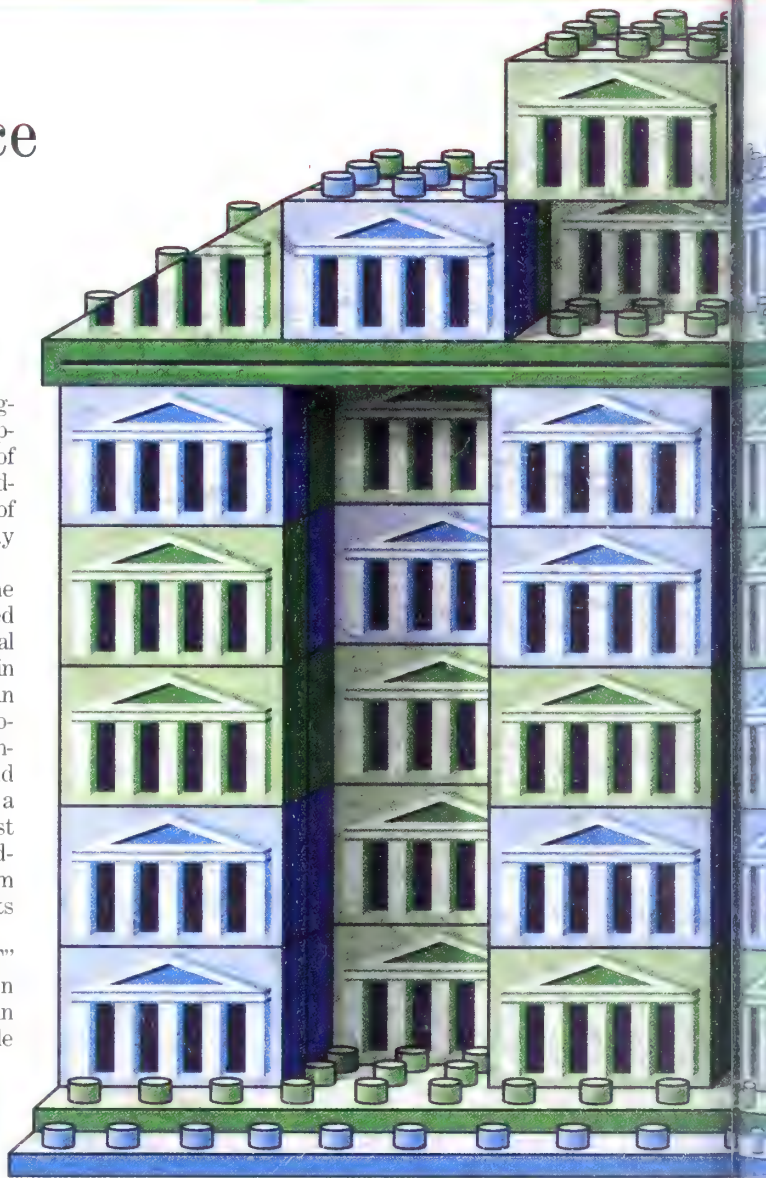
Are megabanks—once unimaginable, now inevitable—better...

The \$1,000,000,000,000 bank. Once, it was unimaginable. But in eight days in April, three eye-popping megamergers have brought the prospect of the first trillion-dollar bank within sight. Suddenly, it seems to be the all-but-certain climax of the cycle of ever-larger combinations that have already reshaped the industry.

As staggering as the \$1 trillion sum may be, the concept is hardly far-fetched. Citigroup, to be formed from a merger of Citicorp and Travelers Group in a deal announced on Apr. 6, will have just under \$700 billion in assets. To get to a trillion, Citigroup co-CEOs-to-be John S. Reed and Sanford I. Weill would only need to put together a deal half the size of the one they just assembled. The combination of NationsBank Corp. and BankAmerica Corp., announced on Apr. 13, creates a \$570 billion giant that promises to become the first truly national bank in the U.S., with red-white-and-blue BankAmerica signs dotting the landscape from California to Carolina. It could reach \$1 trillion in assets in just four years if it grows 10% annually.

This has bankers musing out loud about the "T" word. Says Banc One CEO John B. McCoy, who on Apr. 13 announced his own \$30 billion megadeal to join with First Chicago: "It won't happen in the next couple of years, but in the next five years? Yeah."

But why should it happen at all? In the short run, it's mostly about cost cutting—about wringing efficiencies from traditional banking, now a slow-growth industry rife with overcapacity and declining mar-



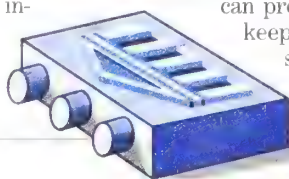
\$1,000,000,000,000

gins. Think steel. In the long run, however, it's about reinventing banks—following the lead of Citicorp and Travelers to create full-service companies that can market a slew of financial services to corporations and consumers.

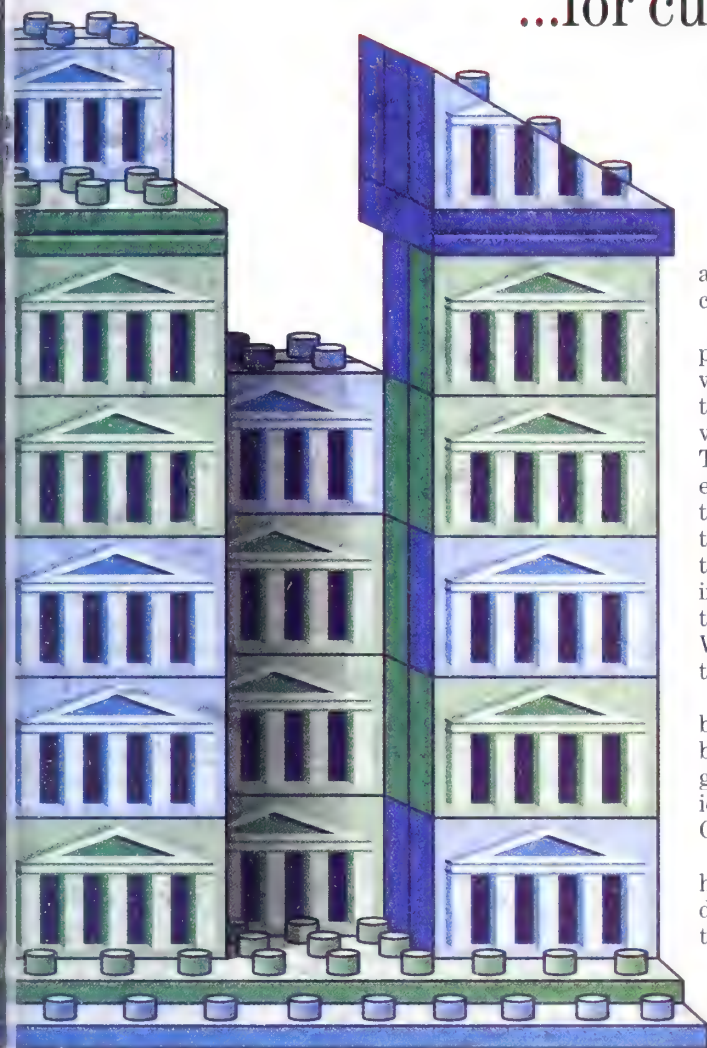
The latter concept—a global financial-services supermarket—has yet to be proven a winner. But investors can easily grasp the benefits of a good old-fashioned industry consolidation. Two big banks merge, combine operations, eliminate jobs and produce a tidy and predictable jump in earnings—and share price. And that new stock

price provides the fuel for the next deal and the next and the next.

This almost self-perpetuating cycle will continue to drive the bank merger wave—and it all but guarantees the creation of a trillion-dollar bank. Indeed, because today's heady bank stock prices reflect growth expectations beyond what mere banks can produce, bank holding companies have little choice but to keep dealing. "Size is driven by the growth requirements shareholders put on their stock," says Peter Davis, partner at consultancy Booz, Allen & Hamilton. "The banks have a growth bogie on their stock."



...for customers, the nation's economy, or even for the banks?

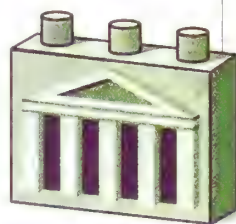


above 55% faces the threat of imminent takeover, according to McKinsey.

At the same time, the race to the trillion-dollar bank is part of a bigger phenomenon. The emerging megabanks will be a geographically diverse conglomeration of traditional banking, mixed with an array of other financial services from stock brokerage to insurance to mutual funds. They will invest heavily in technology that generates efficiencies and allows them to mine data about customers all over the nation—and even overseas—to offer them new products and services. “The type of approach that will come forward—what I would call the global information relationship—is one where a financial institution will have customers both local and global,” says William Randle, an executive vice-president at Huntington Bancshares.

The trillion-dollar players will also introduce national brand marketing to the banking business. As megabanks spend hundreds of millions annually on ad budgets to build nationwide clientele, names like BankAmerica will be right up there with McDonalds, Nike and Coke.

Still, there is as much fear as hope behind the race to the trillion-dollar mark. Conventional banking—taking deposits and making loans—is now a commodity business with paper-thin margins. The Federal Reserve calculates that banks’ share of household fi-



10,000 BANKS

and it's not going away. Look what happened in the days following the first of the first of the three big deals in April. Bruyette & Woods Inc.'s banking index jumped 6%. In megabank deals could provide megareturns: A recent McKinsey & Co. study concludes that these deals will yield efficiencies and even boost competitiveness. The new BankAmerica, for example, says it can trim its \$19 billion in combined expenses by 10% and cut up to 8,000 positions nationwide. McKinsey found that merger mania often drives high-cost, overpriced players out of the market. Indeed, these days, a bank with an efficiency ratio—of costs to revenues—

financial assets has fallen from 90% in 1980 to just over 55% at the end of last year, while mutual funds' have grown from around 10% to more than 44%. Commercial banks now hold only a 28% share of consumer credit, vs. 72% for nonbanks. And banks' share of business credit has fallen from nearly half in 1980 to around 35% today. Meanwhile, electronic commerce looms as a new threat.

“Something called a bank does not have a monopoly on much of anything,” says William McDonough, president of the Federal Reserve Bank of New York. “The financial-services industry is moving toward a true financial services industry

where the major players will offer a full line of financial products."

Hence the deal frenzy. Sure enough, competitors gaped for a moment at the size of BankAmerica, Banc One, and Citigroup deals. But they are quickly laying plans to catch up. Edward E. Crutchfield, who built First Union into the nation's sixth-largest bank as Hugh L. McColl Jr. transformed cross-town rival Nationsbank, could not sleep the night he heard rumors of the BankAmerica merger. Waking at 4:30 the next morning, he consumed news of the deal over coffee and began plotting his next acquisition. "As the shape of the industry now looks to me, we'll have to do something," Crutchfield says. "There are still two or three major acquirers out there and easily 6 to 10 sellers."

Wells Fargo, Mellon Bank, and PNC Bank are mentioned prominently as takeover targets, while Chase Manhattan, U.S. Bancorp, and First Union are seen as wannabe acquirers. Market sources say U.S. Bancorp could make a run at Wells Fargo, and the new BankAmerica ultimately could buy Banc One—provided regulations limiting banks' share of the total deposit market and changed. Wells declines comment, and Banc One officials could not be reached.

Then there's the talk that Chase would make a bid for First Union. "In a world where Citibank and BankAmerica sold out in a week, nothing is unimaginable any more," says David S. Berry, director of research at Keefe, Bruyette & Woods.

While creating a \$1 trillion bank is now plausible—and plotting its strategy on paper is possible—making such a megabank succeed will be an amazing management feat. That's a tall order in the banking business. The sheer scope of such a large and unproven institution is daunting. "The day-to-day reality of pulling this together will be more difficult than currently envisioned," warns Richard Hartnack, vice-chairman of Union BanCal, California's third-largest bank.

To be successful, the megabanks first will have to stall the decline of the conventional banking business by mixing an alchemy of cutting-edge technological wizardry with old-line



McCOLL OF NATIONSBANK

Aggressive marketing, savvy use of technology and cross-selling of financial services will be the key to making trillion-dollar banks work

banking knowhow. They'll have to create nationwide brands at the same time that they try to retain customers of big banks. They'll have to move people away from tellers and automated banking. And they'll have to integrate geographic and culturally diverse enterprises, all while negotiating the tides of competitive and legislative change.

Aggressive marketing, technology, and the cross-selling of financial services will be the key to making a \$1 trillion bank work. Bankers such as McColl and McCoy dismiss any concern about running their huge enterprises. They recognize that they will have to fight off the lethargy and bureaucratic thinking that often afflict companies of such huge scale. But the bankers believe that running a \$1 trillion bank will not be a more complex task than piloting General Electric or General Motors, Exxon, or Coca-Cola.

Yet even among the converted in banking, there is skepticism. "Is it really valid to think that your mortgage customer is going to be any more in the mood for your credit card than they were two weeks ago?" says First Union's Crutchfield. "There has been no shortage of offers. Consumer financial services is just too damn saturated a market. The



FIRST UNION'S CRUTCHFIELD



CHEMICAL'S SHIPLEY



BANC ONE'S MCCOY



CITIGROUP'S REED

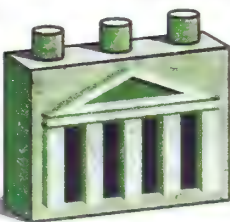
problem is going to be, can you really cross-sell to customers?" Also, the history of bank mergers is not all happy. In many cases, the top-line gains and "synergies" never followed the cost-cutting. And some deals have been troubled from the start. Wells Fargo & Co.'s 1996 acquisition of First Interstate Bancorp is still not completely clicking—even after at least \$150 million in unexpected integration-related write-offs and the loss of at least \$5 billion in deposits. Wells Fargo declines comment.

Indeed, some in the industry see the current race for size as a dangerous excess, driven simply by inflated stock prices and inflated share prices. Richard M. Kovach, chairman of \$88 billion Norwest Corp. in Minneapolis, has undertaken dozens of small acquisitions—but he's skeptical about bank megadeals. The fact that they're big and national doesn't give them any more of a competitive edge," he says. "You get big because you're better. You don't get bigger because you're big."

The dealmakers, of course, beg to differ. "Bigger is indeed better," a beaming McColl boasted at the press conference announcing the BankAmerica deal. "We're not in any business we don't understand. We think we'll add to our product mix." And clearly, size can generate economies. Already, big banks are investing around \$1 billion a year each on technology investments alone, from huge call centers to interactive ATMs. First Union just completed a 2 million-square-foot call center

outside of Charlotte, where its phone banks handle transactions for a fraction of the cost of traditional tellers.

Still, bigness could create its own problems. For example, the BankAmerica deal combines two brokerage firms with a long history of personal and professional animosity: NationsBank's Montgomery Securities and BankAmerica's Robertson, Stevens & Co. "They are Hatfields and McCoys, betrothed by accident," says a gleeful Daniel Case, CEO of San Francisco-based Hambrecht & Quist. "We will be there to pick up all the orphaned customers."



Some corporate customers are also skeptical. "The Nation/BofA deal should benefit us. But I don't see how the combinations like Citicorp and Travelers are going to provide advantages to corporations like us," says William Stavro, treasurer of Mattel Inc. "We deal on one side with commercial banks and see investment banks as completely different. Put them together to create one-stop shop-

ping? I don't think so."

Indeed, the Citigroup partners are attempting an unprecedented merger of unrelated enterprises—with shared power at the corner office, to boot. The plan could be a recipe for a creative renaissance—or the makings of a management debacle.

Another complication: As the megadealmakers labor to combine branch systems, back-office operations, and other functions, they must address a potential computer nightmare—the Year 2000 problem. Y2K, as it's known, was expected to cost Citicorp

AND THEN THERE WERE...?

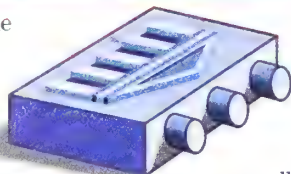
How will the trillion-dollar bank come about? Giants such as Citigroup and Bank of America may continue to buy—in banking and other financial services. Regional heavyweights such as Fleet, Wells Fargo, U.S. Bancorp

and Norwest—buyers now—could become targets. J.P. Morgan and Bankers Trust may also seek deals. Even companies the size of Chase will be under pressure to make megadeals to survive in the megabank era.



\$600 million even before the Travelers deal. And the new BankAmerica's costs could run almost as high. Meanwhile, avoiding a Y2K meltdown will mean diverting money from squeezing technology-related savings from the merged banks.

Consumers also have reason to question the benefits of the megabank. In markets where mergers have led to significant market concentration, consumer advocates say that fees have risen for everything from automatic-teller-machine use to check-cashing to fetching copies of



canceled checks. Corporate customers meanwhile, fear that bigness will mean banks less responsive.

Midsized banks also are bracing for impact of trillion-dollar national rivals. Suddenly, their customers will be inundated with all manner of marketing pleas from new national megabanks—organizations that will also wield the latest greatest technology to bring business to their online banks. To now, Columbus, Ohio-based Huntington BancShares fig-

HOW THE CORPORATE CUSTOMERS SEE IT

Philip B. Livingston knows the downside of bank-merger mania. Catalina Marketing Corp., the \$215 million marketing-services company in St. Petersburg where Livingston is chief financial officer, had a \$150 million credit facility from NationsBank Corp. NationsBank kept \$35 million on its books and syndicated the rest to other banks, including \$25 million to Barnett Banks Inc. Then NationsBank bought Barnett, boosting its exposure to Catalina to \$60 million—\$25 million more than it wanted—so Livingston had to search elsewhere for \$25 million in credit.

The CFO managed to obtain credit from First Union Corp. and Suntrust Banks

Inc. But with NationsBank merging with BankAmerica Corp., Livingston is preparing for another potential fire drill. He says he is a big fan of both banks and doesn't oppose the merger, but bank consolidation concerns him. "Who you can choose from is collapsing unbelievably," he says. "And when I don't have Bank of America competing against NationsBank to get prices down on a new credit facility, that's when we should worry." **"DANGEROUS."** Livingston has good reason to fret about the dwindling number of players in the loan-syndication business. The new BankAmerica will have 17.4% of the business, according to Securities Data Co. Chase Manhattan Corp., the leader, has 27.6%. That will leave two banks with 45% of the market.

Executives at the merging banks insist that their deals will increase competition and benefit bank cus-

tomers. "We think merging helps us meet the competition and continue to be more productive and lower our price," says James H. Hance Jr., vice-chairman and chief financial officer at NationsBank.

Some BankAmerica and NationsBank corporate customers agree. "Because the bank will be more efficient, it will reduce costs both for the corporation and for our owner-operators around the country," says Carleton D. Pearl, senior vice-president and treasurer at McDonald's

Corp. Why? On the cash-management side, McDonald's, a customer of both BofA and NationsBank, will now have one bank that more closely mirrors its domestic store map. On the financing side,

"It will reduce costs both for the corporation and for our owner-operators around the country."

CARLETON PEARL

McDonald's Corp. treasurer



BankAmerica will be able to pool together more of the company's franchisees' loans, speeding up the loan-securitization process.

But other financial executives are not so upbeat. "The logical conclusion is that we'll have six major financial institutions in the U.S.," says William Benedetto, who heads Benedetto, Gartland & Greene Inc., an investment-banking boutique. "To have such a concentrated, national allocation of capital is dangerous."

Some small-business owners also are wary of megabanks. Michael Grela, president of International Aircraft Investors Inc., a \$20 million Torrance (Calif.) aircraft-leasing firm, recently switched his main banking relationship from BankAmerica to Beverly Hills-based City National Bank, which has just \$5.7 billion in assets. "City National has a strong appetite for the kind of business we do," he says.

Mary Barnes, the 72-year-old president of Vita-Erb Ltd., a family-owned soap and shampoo company with about \$1 million in revenues, also has concerns. As an alternate delegate to the Congressional Small Business Summit, she plans to make her worries known in Washington. "I'd like them to make assurances to me that small business will be on a level playing field and that we won't be hurt by these mergers," she says.

BankAmerica says it has pledged \$80 billion in loans to small businesses over the next several years. Still, the new BankAmerica will get roughly 15% of its earnings from middle-market customers and 27% of earnings from corporate-finance business with larger companies. So for some bank customers, big is beautiful, and for others, big may mean finding new bankers.

By Leah Nathans Spiro in New York, with bureau reports

The All New Chrysler Concorde

We started with a clean sheet of pavement.



Well-equipped from \$21,855*

With its sleek design and spirited performance, the all-new Chrysler Concorde quickly separates itself from other large sedans. In the LXi, for example, power is supplied in abundance by the all-new, all-aluminum 3.2 liter 24-valve engine that delivers 225 horsepower with better fuel efficiency** than its predecessor. The Concorde is also equipped with a four-wheel independent suspension and rigid body structure for incredible handling, stability and control. To find out more, simply call 1.800.CHRYSLER or visit our Web site at www.chryslercars.com.



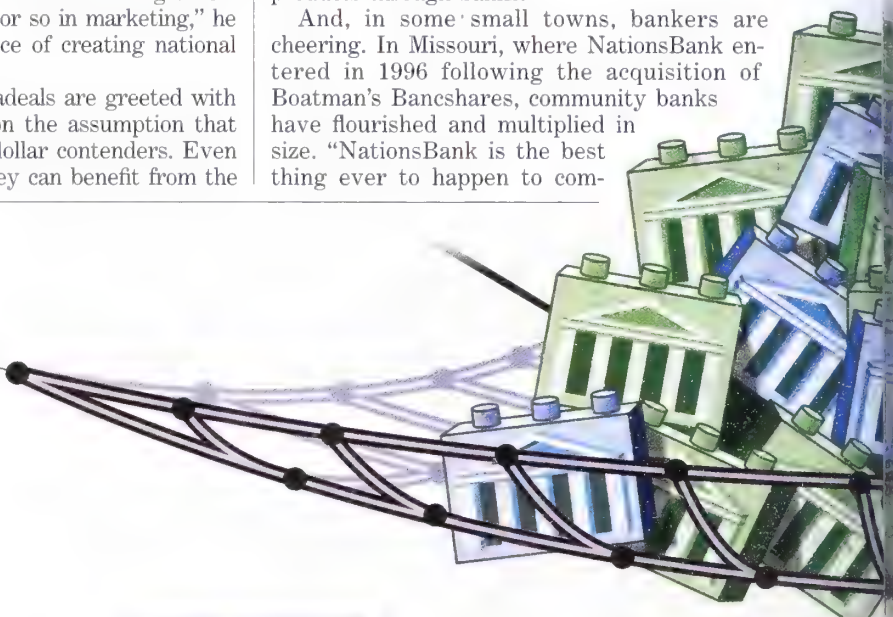
ENGINEERED TO BE GREAT CARS

it had done the smart thing—trying to bring in business by using cutting-edge technology, including the latest ATMs and kiosks that let customers videoconference with bank officials 24 hours a day. Now Randle worries that his bank won't be able to keep up with the new competition. "You're looking at organizations that will spend \$100 million or so in marketing," he says. "They stand a much better chance of creating national and local brands."

In other quarters, however, the megadeals are greeted with glee. Insurers saw their shares soar, on the assumption that some would be snapped up by trillion-dollar contenders. Even if they don't sell out, insurers figure they can benefit from the

megabank trend—by hooking up with the new giants to sell their products. "We're looking forward to working with them," says Ramani Ayer, chairman of Hartford Financial Services Group Inc., which now sells annuities and other insurance products through banks.

And, in some small towns, bankers are cheering. In Missouri, where NationsBank entered in 1996 following the acquisition of Boatman's Bancshares, community banks have flourished and multiplied in size. "NationsBank is the best thing ever to happen to com-



COMMENTARY

By Dean Foust

IF THIS SAFETY NET SNAPS, WHO PAYS?

The spectacle of bankers toasting the latest breathtaking megamergers under the crystal chandeliers of New York's Waldorf-Astoria Hotel is suddenly turning into a weekly ritual. But in the bland hallways of Washington's regulatory agencies, the mind-boggling speed at which banks, brokerages, and insurance giants are consolidating—and changing the face of finance—is cause for anxiety. "This has taken us by surprise," says one stunned regulator.

The regulators have good reason to feel overwhelmed. Bureaucrats trained to monitor banks loan-by-loan may be unable to get their arms around new behemoths like Citigroup and the BankAmerica Corp.-NationsBank Corp. combo, which are racing toward the trillion-dollar barrier. "The marketplace is moving so fast that the government is unable to keep up with it," says William M. Isaac, former chairman of the Federal Deposit Insurance Corp. "Federal regulatory systems are 10 years out of touch."

If the regulators are anxious, then taxpayers should be, too, because they'll be stuck with the tab if these super-

marriages don't work out. To prevent costly bailouts, Washington must rethink how banks are regulated—by shifting more of the risk of failure to private investors, and encouraging the free market to police itself.

HEFT FACTOR. Granted, the U.S. financial industry is far healthier than a decade ago, when Congress shelled out \$150 billion to buy out more than half the nation's thrifts. The ability of commercial banks to expand their branch systems nationwide leaves them less vulnerable to regional slumps and less dependent on one economic sector—like the oil-reliant Texas banks of yore. But given the sheer vastness of the new megabanks—Citigroup will have nearly

\$700 billion in assets—a single merger could bankrupt the taxpayer-funded deposit insurance fund. At a mere \$100 billion, it suddenly looks inadequate.

Despite Citigroup's newfound size, the conglomerate holds just roughly \$100 billion in U.S. deposits. Rampant speculation by aggressive bond traders that Salomon Smith Barney subsidiary's faulty underwriting at the Travelers insurance division could cut deeply into Citigroup's capital structure. Fearful regulators would feel obliged to bail out the parent institution under the long-dormant "too big to fail" doctrine. "If the safety net starting to extend beyond banking, the potential taxpayer exposure has grown," notes Arthur

MONITORING THE MEGABANKS

How regulators...

FEDERAL DEPOSIT INSURANCE Current laws insure depositors against \$100,000 in losses at a failed bank, but regulators often pay more. If the government observes the limits, depositors will be choosier about where they bank.

CAPITAL STANDARDS

Currently, regulators impose lax, non-uniform standards for bank capital. Banks should be allowed to determine how much capital to hold—and are subjected to harsh penalties if losses exceed expectations.

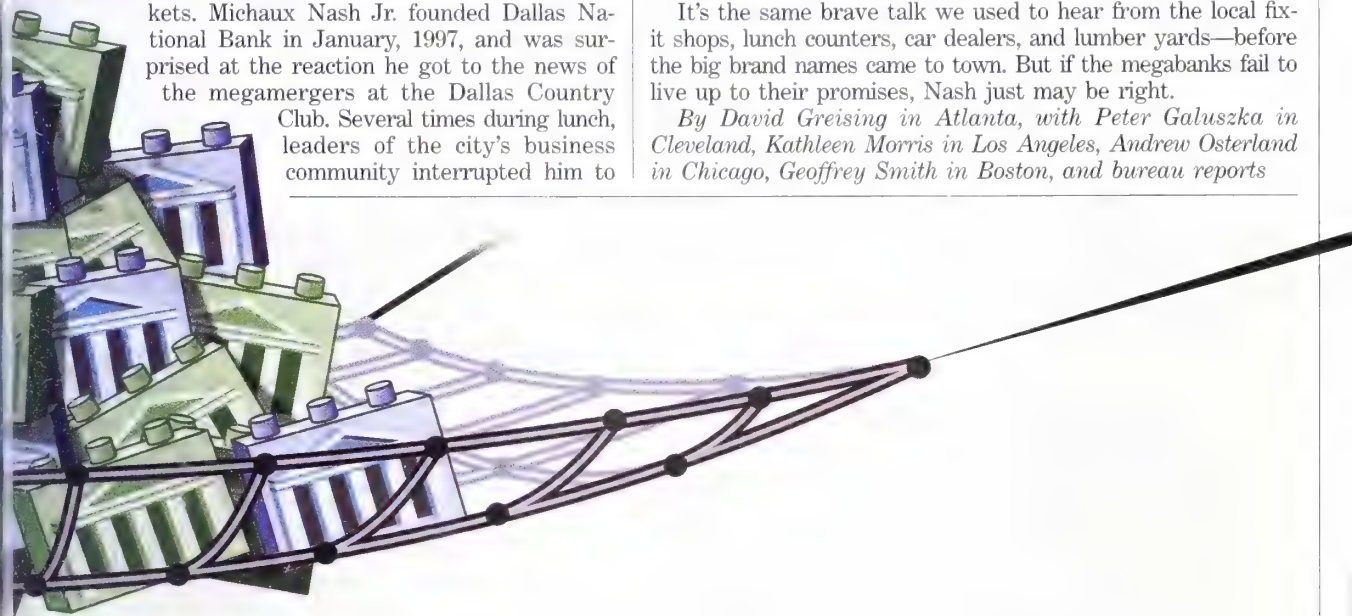
city banking," says John Harlin, president of Century Bank of the Ozarks, a \$125 million bank holding company in central Missouri.

Indeed, even as the industry has consolidated, there has been a flurry of new-bank charters in affected markets. Michaux Nash Jr. founded Dallas National Bank in January, 1997, and was surprised at the reaction he got to the news of the megamergers at the Dallas Country Club. Several times during lunch, leaders of the city's business community interrupted him to

congratulate him on the day's news. "If these mergers keep coming, you'll have to widen your doors for the people to come in," he recalls one person saying. Says Nash: "Let those mergers keep coming. It's fabulous for us locally owned banks. I might have to change my hours to stay open longer."

It's the same brave talk we used to hear from the local fix-it shops, lunch counters, car dealers, and lumber yards—before the big brand names came to town. But if the megabanks fail to live up to their promises, Nash just may be right.

By David Greising in Atlanta, with Peter Galuszka in Cleveland, Kathleen Morris in Los Angeles, Andrew Osterland in Chicago, Geoffrey Smith in Boston, and bureau reports



research director at the Federal Reserve Bank of Minneapolis.

The new conglomerates are considered too important to fail, and government should not continue to add to the risk. Indeed, Congress seriously should think about shifting oversight authority to the group best weed out the troubled institutions: the markets themselves. After the private sector—with its own oversight—should be far more diligent in monitoring behavior that could lead to insolvency than bureaucrats are at the little at stake.

Finally, one of the leading proponents of market-based regulation is Washington's most important regulatory official, Chairman Alan Greenspan. He argues that "rapidly changing technology is rendering obsolescent much of the current bank examination regime," particularly when it comes to overseeing complex products such as derivatives.

Policymakers can start by ending the practice of making whole large depositors in failed banks. Rather, they should be made to suffer losses on one-third of any accounts that exceed the \$100,000 FDIC limit. Corporations and other institutional investors would suddenly be more careful where they parked their cash—and stop supporting shaky banks that pay higher interest rates.

FAT FINES. Another idea floating around the Fed would allow banks to determine the proper capital reserves—presumably less than is now required—to back bank trading in bonds and other securities. The tradeoff: If a bank's trading losses exceeded a certain amount, the bank would be subjected to punitive fines. Brookings Institution economist Robert E. Litan favors requiring all banks to hold uninsured bonds as roughly 10% of capital reserves. This mandate would minimize taxpayer risk by creating a new group of watchdogs—the bondhold-

ers—who could provide "early warning signals" of brewing problems.

A more radical approach would be to replace the government-run system for insuring bank deposits with private insurance. Here's one way it could work: Private guaranty "agents"—say, insurance brokers like Marsh & McLellan Cos.—would serve as the intermediaries between banks seeking private deposit insurance and a syndicate of guarantors, most likely other banks. With on-site inspectors probing the banks' financial health, these private agents would set the premiums paid by banks.

Admittedly, the private markets aren't perfect—witness the herd mentality that sweeps Wall Street periodically. But with capital darting across the globe at the speed of light, it is becoming increasingly difficult for any one country's regulators to keep pace. "The world is going to have to move to private contractual guarantees," says Washington bank consultant Bert Ely. "It's easier to bridge borders through the use of private contracts than with regulators."

As the financial industry moves boldly to change the rules of the game, the regulators need to keep pace with innovative oversight. The bigger these new goliaths of finance get, the greater the consequences if they stumble.

Foust covers banking regulation from Washington.

Handle the new banks

TAXPAYERS

Banks to hold new uninsured part of their capital reserves. To reduce the risk of taxpayer bailout, create new watchdogs—the bondholders—who would care more about safety than profit growth.

PRIVATE BANK INSURANCE SYSTEM

As banking becomes more global and digital, the current system of federal oversight is becoming outmoded. Solution: Allow banks to purchase deposit insurance from private guarantors.

CORPORATE PROFITS

PROFITS TAKE A POUNDING. BUT DO INVESTORS CARE?

They're counting on a rebound in the second half



earnings—although significantly lower than analysts expected—were arriving on schedule, so all was O.K. After all, even Federal Reserve Chairman Alan Greenspan had predicted the weakness.

But are these lower profits really the result of the financial crisis in Asia—a welcome pause to cool the potentially overheating economy, before growth resumes in the second half? Or do they hint at some more significant chinks in the economy's armor, coming as they do at a time when U.S. consumer spending could hardly be more robust?

Indeed, there are troubling signs the profit crunch could get worse. In the wake of Intel Corp.'s report of 36%

lower income, Cowen & Co. managing director Drew Peck hurried to reduce his 1998 and 1999 earnings estimates for the chipmaker after Intel warned its second quarter will be off as well. "There doesn't seem to be any hard evidence that things are going to rebound," Peck says. Other analysts slashed their full-year estimates for Eastman Kodak Co. after it disclosed a sharp 14% drop in consumer film sales. "We've had more warnings than normal from significant companies," says Charles L. Hill, director of research at First Call. "The \$64,000 question is: Do we see a continuation of downward revisions and a broadening in the second quarter?"

"DON'T CARE." So far, Wall Street is clinging to a view of better times later this year. Consensus estimates for profits of companies in the S&P 500-stock index still call for a healthy 12.2% gain in third-quarter earnings and a strong 19.5% gain in the final period. As long as new money continues to flow into

So you think declining profits should be a warning sign that the unstoppable U.S. economy may be coming to a screeching halt? Don't tell investors that. So far this year, they seem to find lower company earnings an exhilarating tonic. And the first quarter's results will give them another big gulp of this strange brew.

With 20% of the companies making up the Standard & Poor's 500-stock index reporting by Apr. 15, initial indications are that first-quarter profits rose an anemic 2% to 3%—compared with analysts' predictions in January of a healthy 10% jump and an actual 30% rise last year. Yet, on Apr. 15, as surprisingly lackluster reports from such highfliers as Compaq Computer, Time Warner, and Coca-Cola rolled in, the Dow Jones industrial average leaped more than 50 points to an all-time high of 9162. For the market, the weaker

CURRENT QTR. SALE
(MILLION)

INDUSTRIALS

ABBOTT LABORATORIES	3,044.9
AK STEEL HOLDING	588.2
ALCOA	3,445.1
ALUMAX	775.3
ARMSTRONG WORLD INDUSTRIES	543.1

BESTFOODS	2,121.4
BLACK & DECKER	1,008.3
BOISE CASCADE	1,489.5
BURLINGTON RESOURCES	432.0
CHRYSLER	16,352.0

COCA-COLA	4,457.0
CONAGRA††	5,385.0
CROWN CORK & SEAL	1,892.4
DOVER	1,148.6
EASTMAN KODAK	2,911.0

ENRON OIL & GAS	199.8
FMC	1,039.0
FRUIT OF THE LOOM	457.2
GENERAL ELECTRIC	22,626.0
GLOBAL MARINE	275.1

GOODYEAR TIRE & RUBBER	3,100.0
HARLEY-DAVIDSON	466.5
INTERNATIONAL PAPER	4,900.0
JOHNSON CONTROLS†	3,007.3
JOHNSON & JOHNSON	5,783.0

NIKE††	2,224.0
NORTHROP GRUMMAN	2,014.0
OWENS CORNING	1,137.0
OWENS & MINOR	798.0
PFIZER	3,339.0

PHELPS DODGE	798.3
WEYERHAEUSER	2,603.0
WILLAMETTE INDUSTRIES	900.1

SERVICES

AMR	4,737.0
AUTOMATIC DATA PROCESSING††	1,309.3
BANKAMERICA	NA
BEAR STEARNS††	1,927.6
BOISE CASCADE OFFICE PRODS.	759.8

DOW JONES	621.5
ENRON	5,682.0
FDX††	3,986.3
FIRST CHICAGO NBD	2,455.0

mutual funds and companies buy back stock at the current breakneck pace, the bull market could be sustained. After all, says H. Vernon Winters, chief investment officer for Mellon Bank Corp. Private Asset Management group, investors "just don't care that earnings are slowing down."

Shareholders in oil companies might be an exception. With crude oil selling for 31% less than a year ago, Big Oil profits are expected to tumble 37% from year ago levels when first quarter results start coming in on Apr. 20, according to consensus estimates tabulated by First Call. Even drillers, the most flush part of the industry, are now tel-

% CHG.	EST. EPS (2/12)	REPORTED EPS	DIFF.	CURRENT QTR. SALES (MILLIONS)	% CHG.	QTR. PROFITS (MILLIONS)	% CHG.	EST. EPS (2/12)	REPORTED EPS	DIFF.	
-8				FIRST UNION	NA	NA	587.0	+16	0.89	0.90	+0.01
+10	0.77	0.76	-0.01	FLEET FINANCIAL	NA	NA	323.0	-3	1.23	1.21*	-0.02
-18	0.49	0.47	-0.02	FOOD LION	2,305.5	+1	55.2	+27	0.12	0.12	—
+32	1.18	1.24	+0.06	GANNETT	1,199.9	+11	342.9	+154	0.55	0.56*	+0.01
+65	0.66	0.81	+0.15	GRAINGER (W. W.)	1,057.1	+7	57.2	+5	1.15	1.16	+0.01
+2	1.12	1.15	+0.03	HERTZ	898.8	+2	35.4	+80	0.23	0.33	+0.10
+14	0.44	0.44	—	KROGER	6,388.8	+4	107.3	+16	0.41	0.41	—
NM	0.24	0.33*	+0.09	MBNA	NA	NA	149.4	+21	0.29	0.28	-0.01
NM	-0.01	-0.18	-0.17	McGRAW-HILL	703.4	+8	20.1	+34	0.17	0.20	+0.03
-63	0.37	0.27	-0.10	MERRILL LYNCH	9,166.0	+23	518.0	+11	1.12	1.30	+0.18
+2	1.45	1.60	+0.15	MGIC INVESTMENT	244.3	+19	94.0	+30	0.75	0.81	+0.06
-13	0.35	0.34	-0.01	MORGAN STANLEY DEAN WITTER	7,585.0	+16	691.0	+21	1.10	1.10	—
-4	0.36	0.30	-0.06	MORGAN (J. P.)	NA	NA	237.0	-44	1.93	1.80*	-0.13
+7	0.37	0.29	-0.08	NATIONSBANK	NA	NA	497.0	-42	1.07	1.20*	+0.13
+15	0.41	0.40	-0.01	NORWEST	NA	NA	367.7	+14	0.47	0.47	—
+51	0.73	0.69	-0.04	PAINWEBBER GROUP	1,805.1	+18	120.7	+20	0.66	0.77	+0.11
+17	0.21	0.17	-0.04	PNC BANK	NA	NA	269.3	+1	0.86	0.87	+0.01
+26	0.80	0.75	-0.05	ROADWAY EXPRESS	621.7	+5	6.6	+20	0.32	0.32	—
+38	NA	0.43	NA	SERVICE MERCHANDISE	594.2	-13	-24.1	NM	-0.27	-0.24	+0.03
+13	0.57	0.57	—	SLM HOLDING	840.8	-9	139.0	+20	0.75	0.80	+0.05
-13	0.42	0.39	-0.03	SUNTRUST BANKS	NA	NA	180.9	+12	0.83	0.85	+0.02
+4	1.16	1.11	-0.05	SUPERVALU†††	4,297.5	+10	51.6	-3	0.83	0.86	+0.03
+11	0.29	0.29	—	SYSCO††	3,711.8	+7	63.6	+3	0.20	0.19	-0.01
+121	0.36	0.25	-0.11	TIME WARNER	3,137.0	+3	-62.0	NM	-0.19	-0.25	-0.06
NM	0.55	0.56	+0.01	U. S. BANCORP	NA	NA	328.5	+12	1.38	1.40*	+0.02
+11	0.76	0.73	-0.03	TECHNOLOGY	1,445.4	-3	145.4	-38	0.75	0.72	-0.03
-69	0.40	0.25	-0.15	ADVANCED MICRO DEVICES	540.9	-2	-55.8	NM	-0.13	-0.39	-0.26
NM	1.48	1.52*	+0.04	APPLE COMPUTER†	1,405.0	-12	55.0	NM	0.15	0.38	+0.23
-81	0.16	0.16	—	COMPAQ COMPUTER	5,687.0	+8	16.0	-96	0.35	0.01	-0.34
+35	0.17	0.17	—	GENENTECH	244.1	+1	41.0	+30	0.27	0.32	+0.05
+15	0.53	0.53	—	INTEL	6,001.0	-7	1,273.0	-36	0.93	0.81*	-0.12
+19	0.67	0.70*	+0.03	MOTOROLA	6,886.0	+4	180.0	-45	0.50	0.30	-0.20
+305	0.48	0.43	-0.05	SEAGATE TECHNOLOGY††	1,675.0	-33	-128.5	NM	-0.04	-0.10*	-0.06
+66	0.24	0.20	-0.04	UNISYS	1,649.7	+8	62.7	+225	0.11	0.14	+0.03
+7	0.74	0.77	+0.03	UTILITIES & TELECOM	1,411.3	+14	141.3	-44	0.88	0.92	-0.25
+91	2.39	3.24	+0.85	AMERITECH	4,133.0	+7	492.0	-8	0.54	0.44	-0.10
+16	0.63	0.64	+0.01	GTE	5,885.0	+11	142.0	-79	0.67	0.15*	-0.52
+7	1.15	1.17	+0.02	ILLINOVA	575.4	+1	23.0	-48	0.19	0.32	+0.13
+1	1.03	1.15	+0.12	PG&E	4,353.0	+29	139.0	-20	0.46	0.36	-0.10
+18	0.27	0.27	—	TECO ENERGY	467.8	+4	30.8	-39	0.42	0.40	-0.02
+37	0.32	0.35	+0.03								
-4	0.67	0.65	-0.02								
NM	0.64	0.09	-0.55								
+1	1.28	1.30	+0.02								
†Second-quarter results NM = not meaningful											
††Third-quarter results NA = not available											
††† Fourth-quarter results *EPS adjusted for special items											
DATA STANDARD & POOR'S COMPUSTAT, A DIVISION OF THE MCGRAW-HILL COMPANIES EARNINGS ESTIMATE DATA PROVIDED BY I/B/E/S INTERNATIONAL INC., NEW YORK, NY I/B/E/S IS A REGISTERED TRADEMARK OF I/B/E/S INTERNATIONAL INC.											

†Second-quarter results
NM = not meaningful

††Third-quarter results
NA = not available

†††Fourth-quarter results
*EPS adjusted for special items

DATA: STANDARD & POOR'S COMPUSTAT A DIVISION OF THE MCGRAW-HILL COMPANIES
EARNINGS ESTIMATE DATA PROVIDED BY I/B/E/S INTERNATIONAL INC., NEW YORK, NY I/B/E/S IS A REGISTERED TRADEMARK OF I/B/E/S INTERNATIONAL INC.

ing their outlook. "Right now, the [oil] market is better than it has been," says C. Russell Luigs, CEO of offshore driller Global Marine Inc. Looking into the future, you may see a softening."

Meanwhile, analysts are slashing estimates for technology companies, long markets' little engines that could. Call's second-quarter profit outlook for these companies has been slashed to a low, from January estimates of increases of 15%. Another warning sign: chemical industries such as paper, chemicals and metals, are expected to see earnings actually drop 1% this quarter. Economists see profits continuing to

be squeezed between a flood of low-cost imports and rising labor costs. Some economists, such as James O'Sullivan at J.P. Morgan & Co., now expect gross domestic product, which grew 4% in the first quarter, to increase by only 1% in the third and fourth. "If you look at corporate profits, there is a lot more than Asia going on," O'Sullivan says.

FED JITTERS. And now, there are jitters about a change of heart at the Federal Reserve. Salomon Smith Barney Inc. economist David Hensley says he is beginning to worry that rather than cutting rates this year because of the Asian financial crisis, the Fed could actually raise rates because of unstop-

pable consumer demand. An increase in unemployment or a drop in the market could prevent that, but despite continuing downsizing by major companies the unemployment rate seems stubbornly low and the market stubbornly high.

Of course, this is a stock market that continues to defy the rules. So despite profit margin pressures, rising wage costs, and competition from imports, stocks could continue to float on a sea of liquidity. Whether it's investors padding retirement plans or corporate chiefs boosting buybacks, stocks are still the best game in town.

By Gary McWilliams in Houston and Frederick F. Jespersen in New York

MANAGEMENT

LOST IN SPACE AT BOEING

Post-merger clashes throw the aerospace giant off-course

Marriage counselors always warn young couples that money troubles are the biggest threats to a happy union. Boeing Co. can tell you it's not so good for corporate marriages either.

Almost from the time Boeing completed its merger with McDonnell Douglas Corp. last August, the company has been racking up writedowns caused by production problems and product cancellations. On Apr. 27, Boeing execs are bracing for their first post-merger shareholder meeting—at which investors will be asking why the parts shortages and assembly-line glitches that the Seattle aerospace giant promised to clean up six months ago still persist. On Apr. 9, Boeing announced a new \$350 million charge, bringing the tab for the production disasters to nearly \$3 billion. Boeing's stock, now at 53, is nearly 12% below where it was when the \$13 billion McDonnell deal closed.

PUBLIC SPATS. It all adds up to a lot of stress in the combined corporate family. For months, President Harry C. Stonecipher, the hard-nosed former McDonnell Douglas CEO who joined Boeing in the merger, has disagreed—at times, in public—with Ronald B. Woodard, head of Boeing's commercial aviation unit, over the cause of the problems. Before Stonecipher came aboard, Woodard was in line to be president, and the two clashed from the start, insiders say. Stonecipher, they add, even tried to pin blame on Boeing's popular Chairman and CEO Philip M. Condit.

The potential for internecine war has kept the rumor-mill working overtime both on Wall Street and at Boeing. Indeed, earlier this year Condit publicly denied reports that Woodard would be fired—or that he himself would be stepping down and former CEO Frank Shrontz would return.

Condit, Stonecipher, and Woodard all deny any tensions and say they work

well together. And in a recent interview, Stonecipher and Condit seemed in sync in their views. But Boeing's directors—a third of whom came from McDonnell Douglas—are growing impatient. The board doesn't want any more surprises, say observers and insiders, and further large charges could force Woodard out. "A lot of investors think that there have been all these problems, and yet no one has lost their job," says Bill Whitlow, manager of Saveco Northwest Fund, which has \$4 million in Boeing stock. On the other hand, customers aren't looking for more disruption. "I would hate to see any shuffle in management, given that we're the ones who would be the recipients of the consequences," says Gordon M. Bethune, CEO of Continental Airlines Inc., which is slated to take 15% of Boeing's output this year.

In a joint interview with *BUSINESS WEEK*, Condit and Stonecipher said they won't make a scapegoat of anyone. But they're not ready to declare that their problems are behind them, either. "A lot of issues started a long time before [last fall], so you can't snap

your fingers and say: 'Let's shape here,'" says Condit.

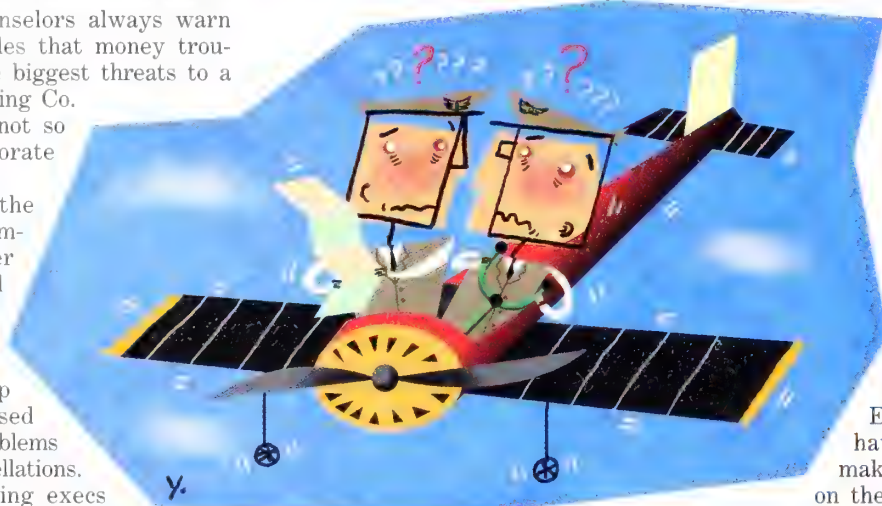
Today, Condit and Stonecipher show a united front and say they're working together to shift Boeing's culture. In the past, Boeing's focus was on designing the most advanced planes, says Condit, and cost was a secondary issue. But airlines are balking at higher costs and

Boeing is now competing on price with rival Airbus Industrie to snag commercial market share.

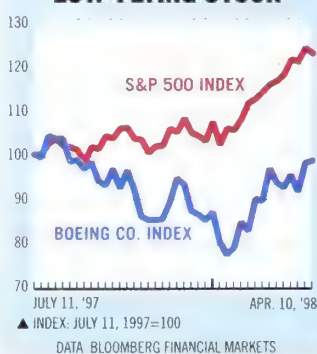
But in straining to fill 1,750 orders for new planes, Boeing has had costs spin out of control. Six months after the problems appeared, work is still being done out of sequence, union officials say. And demands from U.S. and European regulators have forced Boeing to make expensive redesigns on the new 737. "These production problems just go on and on," sighs Byron Callan, an aerospace analyst at Merrill Lynch & Co. "I don't think management knows what's really happening on the factory floor."

Part of the problem is the cultural clash at the top, says Jon B. Kutler, president of Quarterdeck Investment Partners Inc., a Los Angeles aerospace investment bank. Stonecipher, who spent 26 years at General Electric Co. building a reputation there and at McDonnell Douglas as an aggressive, cost-oriented executive. Woodard and Condit, two career Boeing vets, come from a tradition that stresses more collaborative problem-solving.

Stonecipher's forceful style has made him a lightning rod within Boeing ranks. Analysts and union leaders accuse Stonecipher of posturing for Wall Street. In December, Stonecipher announced that Boeing planned to slim down by 12,000 employees and cut costs. But with the plant floor problems, Boeing actually holding employment levels steady and only recently stopped hiring. "They brought Stonecipher in to whip it into shape, but instead he's pissed everyone off," says a machinist



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Boeing's Everett (Wash.) plant. Stonecipher says it's his job to be the tough guy and take the heat for Condit. He argues that he has restrained himself: The most difficult "part in this whole thing has been not slaying people," he says. Condit, for his part, says he leans on Stonecipher. "One of the things that has got me through was that I could walk down the hall and put my head on Harry's desk and say: 'Aaargh,'" he says.

The groaning isn't likely to end until until the production problems do. Woodward says the company is "bouncing back," and points to improved production schedules on the 747 and 767 assembly lines. Still, in commercial aviation, which accounts for 56% of company revenues, Boeing will lose money on at least the first 400 new 737s. That means it won't show profits from that plane until 2000, when the first batch is completed.

As a result, Boeing's stock will continue to languish and could even fall more, says Prudential Securities Inc. analyst Nicholas P. Heymann, who turned negative on Boeing when the production problems surfaced last fall. Not quite the news to make shareholders smile when they gather in St. Louis.

*By Aaron Bernstein in Washington
Andy Reinhardt in Costa Mesa, Calif.
and Seanna Browder in Seattle*

COMMENTARY

By Wendy Zellner

BOB CRANDALL: AN AMERICAN GLADIATOR

The airline industry, long the playground for oversize egos and larger-than-life characters, is losing one of its most colorful personalities. Robert L. Crandall, chief executive of AMR Corp. and American Airlines Inc. since 1985, is retiring in May at age 62. He's even relinquishing his board seat. Crandall's immediate plan: to cross the Atlantic on his new 48-foot sailboat.

To his credit, Crandall is sailing off at a good time for him and American. After years of downsizing, the company is now enjoying record profits and a record stock price. It's back at the top in on-time performance. And it's poised to cement powerful alliances with airlines in Europe, Latin America, and Asia.

But for all his strengths—and Crandall has many—he may not be the man to lead in a world where sharing power with partners and with labor will be more critical. "Bob ran the company in a way where he knew best. As a result, American lost out on a whole bunch of opportunities," says one former American executive. **"HE'LL EAT YOU ALIVE."** But love him or hate him—and the profane, hard-charging Crandall always engenders strong feelings—he has left an indelible stamp on American and the industry. His innovations are legendary: frequent-flier programs, sophisticated computer reservation and pricing systems, and huge hub-and-spoke networks. After deregulation came to the airline industry in 1978, he cut costs with a then-novel,

two-tier pay scale that put new hires on a lower salary track.

From 1983 to 1988, he plowed some \$7 billion back into the company for new planes and built American from an also-ran to an industry powerhouse. "If there's anybody who has shaped this industry and made American what it is today, it's Bob Crandall," says Continental Airlines Inc. CEO Gordon M. Bethune. As former

er airline exec were to participate in a singing contest at an industry conference. Crandall not only rewrote the song after being told not to but reassigned Kelleher from bass to tenor.

On the other hand, Crandall's tendency to approach every situation as a contest with winners and losers has sometimes cost the company dearly. American has suffered two painful strikes in five years, in good measure because of Crandall's miserable relations with his labor unions. He also alienated other airline executives. He had a smart plan to simplify the industry's unwieldy fare system in 1992, but it provoked a bloodbath of price-cutting: Mistrustful rivals felt "if Bob's for it, there must be something wrong," recalls one former exec.

Some fear that under Crandall's affable successor—President Donald J. Carty, 51—the airline could lose some edge. But Carty's more diplomatic style—he often plays mediator between Crandall and his subordinates—may help the airline on some crucial fronts. In September, American begins labor talks with flight attendants, who struck in 1993 for five days. And in Washington, its proposed alliance with British Airways PLC—a linchpin in its competition with other airline partnerships—faces intense regulatory scrutiny. Now that he's emerging from Crandall's shadow, Carty has a chance to show he's the right man at the right time. Just as Crandall was.

Zellner covers American Airlines for BUSINESS WEEK in Dallas.



POWERFUL PILOT: Crandall's innovations are legendary

American Chairman Albert V. Casey, who tapped Crandall in 1980 to serve as the airline's president, sums him up: "You never want him on the other side. He'll eat you alive."

Crandall prevailed by force of will and obsessive attention to detail. One former executive recalls a flight with Crandall years ago from Dallas to New York. Crandall was given a salt shaker with a Continental logo. He dumped the salt on his tray, angrily pocketed the shaker, and later sent it to the head of the catering business with a pointed note. Southwest Airlines Co. CEO Herbert D. Kelleher recalls the time he, Crandall, and another

ISTBUSTERS

IE SMELL OF BLOOD 'INTEL

ling that suggests it's a monopoly could embolden the feds

While everybody was watching Microsoft Corp.'s battle in the Beltway, a federal judge in Alabama ped a bombshell on the other half ie "Wintel" duopoly. On Apr. 10, District Judge Edwin L. Nelson that Intel Corp. likely violated U.S. trust law when it withheld products

idly turn into a stream," he says. A surge of private litigation could even cause the FTC to shift the focus of its probe. The agency won't comment on its inquiry, but Intergraph staffers say the FTC has interviewed the company about its complaints. The FTC is looking at whether Intel is leveraging its domi-

el is known for its legal impregnability, t "once that wall is broken, a trickle can idly turn into a stream"

technical information Intergraph Corp., a er of computer work- ons. Nelson's prelimi- injunction, the first to label Intel an abu- monopoly, could lead urther legal troubles he chip giant—specifi- by giving the Feder- ade Commission more over in its investiga- into the company's iness practices. "It's a damaging ruling," says Peck, a Cowen & Co. ana- "The aftershocks could be ex- ordinarily strong"

ONSCIONABLE." Intel insists the e is wrong. But legal experts think ruling could embolden the FTC, a is expected to decide by this sum- whether to launch a formal action. as Orrin Hatch [with his Senate iary Committee hearings] gave the ce Dept. support in its fight against osoft, so this decision gives the FTC ort] against Intel," says Howard e of Washington's Drinker, Biddle eath, an ex-staffer at the FTC who worked on the Intel inquiry. he ruling could also encourage other d-be litigants. Intel customers and s have typically shied away from onting the company, which is n for its aggressive legal tactics. now they may smell blood. Morse pares it to tobacco lawsuits: "Once wall is broken, a trickle can rap-

nance in processors into adjacent markets and at its use of nondisclosure agreements on future products to keep customers in line. Nelson called Intel's withdrawal from such agreements with Intergraph "unconscionable."

The key element in the ruling: Nelson said Intel chips have become an "essential facility," a legal standard that, for instance, requires the owner of the only bridge into a town to offer equal access to all traffic. If upheld, Pentium chips would be treated like any public asset. Many legal analysts suspect Nelson went too far. But "if a federal court has already found that Intel's chips are an essential facility, it makes it easier for the FTC," says Art

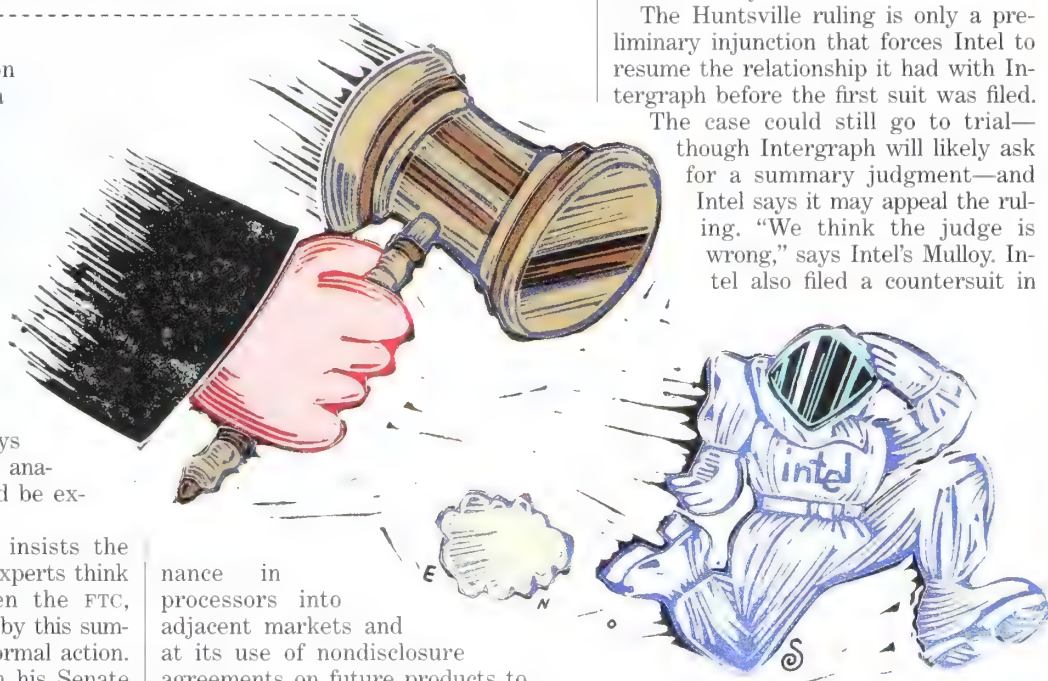
Amolsch, editor of newsletter *FTC Watch* in Washington.

Such a far-reaching impact wasn't on Intergraph's radar when the Huntsville (Ala.) company filed its patent claim last November. The \$1.2 billion workstation maker argued that it owned patents on technology used in Intel's Pentium Pro and Pentium II processors. "Intel wanted access to the patents we had, and they were unwilling to pay," says James W. Meadlock, Intergraph's CEO. Intel stopped supplying Intergraph with technical data and early samples of its upcoming processors—a move Intergraph says cost it \$100 million in lost sales in the fourth quarter. So in December, Intergraph added antitrust claims to its suit.

Intel's version of events differs greatly: It says the patents aren't valid. What about cutting off shipments to Intergraph? "It's prudent not to ship intellectual property to a company that is going to sue you," says spokesman Chuck Mulloy.

The Huntsville ruling is only a preliminary injunction that forces Intel to resume the relationship it had with Intergraph before the first suit was filed.

The case could still go to trial—though Intergraph will likely ask for a summary judgment—and Intel says it may appeal the ruling. "We think the judge is wrong," says Intel's Mulloy. Intel also filed a countersuit in



'97 that was stayed, pending Nelson's decision.

Will the Huntsville ruling tame the notoriously aggressive Intel? Or stop the kind of behavior that, according to former FTC Commissioner Christine Varney, prompted the agency to probe the chip giant in the first place? Maybe not. But even if the smaller company hasn't felled the Goliath, it has landed a stunning blow.

By Andy Reinhardt, with Robert D. Hof, in San Mateo and Mike France in New York

MARKETING

WOULD YOU SPEND \$1.50 FOR A RAZOR BLADE?

Gillette is betting a billion that the answer is yes

In April, 1995, Gillette CEO Alfred M. Zeien went to his board with an audacious proposal. He wanted the green light to develop a new triple-bladed razor that would require "the biggest capital investment in our history," he recalls. Not surprisingly, the directors—including Warren E. Buffett—asked to see the goods. But Zeien refused, holding firm even after one director argued that "we have the right to ask any question we want." It wasn't until last November, when the Mach3 was rolling off a production line in South Boston, that the board finally got to try Zeien's brainchild.

After more than a decade of work and \$750 million in development and tooling costs, the Mach3, introduced on Apr. 14, will arrive in stores starting July 1. That's a staggering sum for a razor: roughly equal to the global razor-blade sales of number two Warner-Lambert Co., which owns Schick and Wilkinson Sword. Zeien vows that the investment—plus \$300 million more for advertising and marketing over the next 15 months—will propel Gillette Co. and its stock into the millennium.

TEST FLIGHTS. That means convincing millions of men—and eventually, millions of women—that the gee-whiz technology that Gillette has poured into Mach3 produces enough smoothness and comfort to justify an eye-popping 35% price increase over the SensorExcel, Gillette's current top-of-the-line product. That's the most aggressive price hike Gillette has ever attempted for a new razor, and it comes at a time when most consumer-products companies struggle to pass on even single-digit increases. "It is a hell of a risk," argues Jeffrey Hill, managing director of Meridian Consulting Group in Westport, Conn., since "consumers are far more satisfied" with today's shaving products than they were when Gillette launched Sensor in 1989. Investors agreed: Gillette's stock slipped \$6, to \$118, by Apr. 15, the day after Mach3 was announced.

Will it fly? John M. Darman, Gillette's vice-president of male shaving, brags

that the ad campaign, heavy with *Top Gun* imagery, is "off the charts" in its ability to motivate men from France to Florida to "take Mach3 for a test flight." Amy Low Chasen, an analyst at Goldman, Sachs & Co., believes that the Mach3 will generate annual revenues of \$1 billion by 2001.

But men will only stick with Mach3 if it lives up to the hype. Gillette has applied for 35 patents on Mach3 and the manufacturing process used to make it.

REACHING MACH3

1985 Serious research begins on developing the first new edge for Gillette's blades since 1969.

1988 Gillette researchers try arranging three blades in a progressive alignment, meaning the first blade sticks out less than the second and third blades.

1992 An advanced prototype, Manx, beats Sensor Excel, Gillette's most advanced razor, in shave tests

1995 Gillette's board green-lights Manx development.

MID-1996

Gillette engineers develop a method of assembling Manx's cartridge that is three times as fast as SensorExcel production.

FALL, 1997 Board approves final stage of the \$750 million investment. Production begins.

APR. 14, 1998 Mach3 unveiled.

DATA: GILLETTE CO., BUSINESS WEEK

In addition to its three blades, Mach3 features six other innovations, including a new method of loading cartridge and a new blade edge, applied atom by atom with chipmaking technology.

It could be technological overkill, though. Zeien says that even at Gillette, "a lot of people argued we should simply put out a Sensor3 product." That would have cost less—and allowed Gillette to build on the installed base of 400 million Sensor razor handles already sold.

Still, he believes that an all-new triple-blade razor will pay off handsomely. As early as 1992, Gillette's researchers already had a "Manx" prototype that in tests "was beating the pants off our best product, SensorExcel," says Thomas L. Gallerani, vice-president of Gillette's shaving technology lab. Zeien then insisted that Manx would have to have a radically new blade edge, too.

This edge, known as DLC—for diamond-like carbon coating—is three times stronger than stainless steel and allows Gillette to use much thinner blades. Problem is, DLC also helps blades last longer.

To help combat the problem, Mach3 features a blue "indicator strip" that will fade to white as the blades are used and signal when it's time for new ones. Darman concedes that fewer cartridges will be sold. "Our best guess is that consumption will fall 10%," he says. However, if he's wrong and consumption drops much more than that, Mach3 could be a disappointment.

SLO MO. The Mach3 is so complex that Gillette has developed a new manufacturing process for it. Eventually, the plant should spit out 600 cartridges a minute, three times more than the process used for Sensor, says Michael T. Cowhig, the senior vice-president for manufacturing who oversees Mach3. But six months into production, the process is still running at just 250 cartridges per minute.

Will Mach3 move as fast as Gillette expects? Even if consumers agree that it's a big improvement over Sensor, will they like it enough to pay \$1.50 for a cartridge—the biggest premium in shaving history? They'll be paying for high tech and the promise of fewer nicks and less irritation. Or, for \$2 they can still buy a 10-pack of disposable razors.

By William C. Symonds



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COMPAQ

IRELAND

READY TO BLAST OUT OF THE BOG

Northern Ireland's peace deal may lure investments and jobs

The historic Apr. 9 peace deal between the governments of Britain and Ireland and the main Northern Ireland political parties was a watershed. But as the North's party leaders straggle back from their Easter celebrations, they are facing an equally difficult challenge: how to keep up the momentum.

One important way, all parties agree, is to attract investment and create jobs in Northern Ireland—to emulate the success of the Irish Republic to the south, which has been an investment magnet in recent years. Once a backwater, the Republic of Ireland has been enjoying robust growth. An economic boom in the North would soak up pockets of unemployment there and be a big incentive for paramilitary groups to put away their rifles and plastic explosives for good.

It won't happen overnight. Businesses have been disappointed when violence erupted after earlier cease-fires. "We've seen it all before, and we don't have any trust in it," says Sonny Baird, who runs Internet Café in central Belfast.

SOUTHERN EXPOSURE. Still, executives say this time could be different. All the main parties—including Gerry Adams, president of Sinn Féin, the political wing of the Irish Republican Army—are on board. The British and Irish Prime Ministers, Tony Blair and Bertie Ahern, have their prestige on the line, and President Clinton is also involved. "I think we will see an increase in business activity building up in the coming years from both tourism and investment," says Ronnie Kells, group chief executive of Vister Bank Ltd., the Irish arm of Britain's National Westminster Bank.

Subtle changes in the political and economic climate helped pave the way for

this deal. Despite the "troubles," Northern Ireland has taken a cue from its southern neighbor in trying to lure investors—with some success. Since 1993, Northern Ireland has attracted about \$2.5 billion in foreign investment. Foreign

cord that it is ready to pour \$47 million more into its facilities at Monkstown in the north, where some 1,200 employees design and manufacture fiber-optic transmission gear. "Peace and stability will remove a huge obstacle for potential investment for Nortel and other companies," says Robert J. O'Brien, a Nortel vice-president.

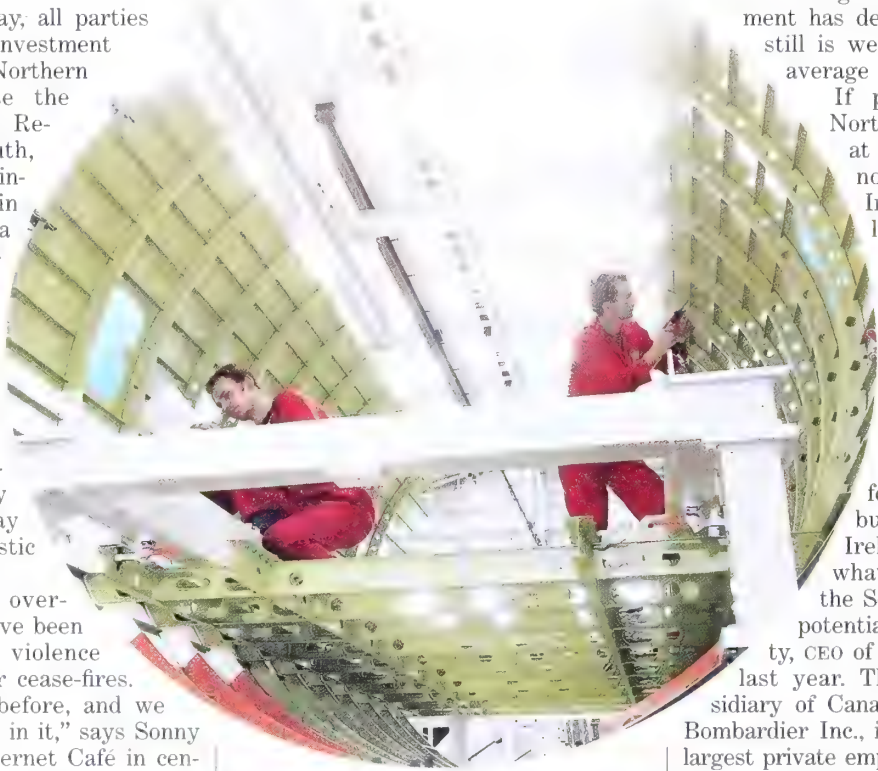
Foreign investment flows, as well as Britain's spending about \$3,000 annually for each of the 1.6 million inhabitants, have helped give Northern Ireland slightly faster economic growth than Britain as a whole in recent years. But it remains the poorest region in the nation, with a gross domestic product per person of \$14,400 a year—81% of the British average. And while unemployment has declined, its 7.9% rate is still well above the British average of 4.8%.

If peace prevails, the North will have a chance at duplicating the economic revival of the Irish Republic, where living standards rival those in England, Scotland, and Wales. The 8.2% economic growth rate racked up by the Republic of Ireland last year was the highest in the European Union.

Certainly, some foreign companies are bullish on Northern Ireland. "We have seen what has been done in the South, and we see the potential here," Roy McNulty, CEO of Short Brothers, said last year. The company, a subsidiary of Canadian airplane maker Bombardier Inc., is Northern Ireland's largest private employer. A Bombardier spokesman says the latest accord "bodes well" for the company's operations there.

Whether the North can attract significant new investment, though, remains to be seen. Sterling has strengthened 14% against the Irish pound in the past year, so it's cheaper to go south. As a result, Northern Ireland will have to offer incentives. Northern politicians have every reason to be accommodating to business, since the peace accord turns over more responsibility for the economy to them. Gerry Adams proved a crack fund-raiser for Sinn Féin. Now, the world can see how good he is at wooing foreign investors.

By Stanley Reed in London, with Joseph Weber in Toronto



TAKING OFF

In Belfast, employees for Short Brothers assemble fuselages for Bombardier's Global Express aircraft

companies such as Seagate Technology Inc. and Emerson Electric Co. now employ about 11,000 people, 11% of the total manufacturing workforce.

Multinationals that have invested have found a well-educated, hard-working labor force. Northern Telecom Ltd., which has big investments in both Irelands, is sufficiently pleased with the latest ac-

EDITED BY PAT WECHSLER

INFOTECH PACKS A HEFTY WALLOP

NOW IT'S OFFICIAL: THE U.S. IS in the midst of a Digital Revolution, transforming the way companies do business and cutting costs. On Apr. 15, the Commerce Dept. issued a sweeping report on how information technology is transforming the economy. Infotech, now at more than 8% of domestic output, is responsible for one-quarter of the economy's growth and provides 7.4 million jobs at an average wage of \$46,000—64% higher than the private sector overall, Commerce found. Meanwhile, on Apr. 14, the revolution got a boost from Vice-President Al Gore, who announced a partnership with Qwest Communications, Cisco Systems, Nortel, and

122 universities to create a next-generation superfast research network.

WASHINGTON IS COOL TO THE YEN

TREASURY SECRETARY ROBERT Rubin feels Japan's pain. But he's not promising any action to bolster the yen. After meeting in Washington with Japanese Finance Minister Hikaru Matsunaga on Apr. 15, Rubin said that he "shared his concern" about the yen's "excessive depreciation" to a recent six-year low of 135 yen to the dollar. Both ministers pledged to "cooperate closely as appropriate" to bolster the currency. But that and 292 yen will get you a cup of latte: The U.S. has pointedly remained aloof from the Bank of Japan's recent massive buying spree.

CLOSING BELL

GOING UP

Asia and cold weather may spell woes for United Technologies. But its stock hit an all-time high of 98% on Apr. 14 and closed at 95% the next day. Why? Wall Street loves cost-cutting. On Apr. 13, UT's Otis Elevator announced a 3% workforce cut and the closing of 13 engineering centers—moves analysts say will drive margins into double digits. Belt tightening is also expected at air-conditioner maker Carrier. But the Asian building boom UT was counting on for growth seems stuck between floors.



BLENDED: PENNZOIL AND QUAKER STATE

PENNZOIL, WHICH RECENTLY fought off a hostile takeover bid, is spinning off its consumer automotive products and Jiffy Lube businesses. The new company will then merge with rival Quaker State to form the nation's largest motor-oil concern. Pennzoil shareholders will hold 61% of the newly formed \$3 billion company, which will control 37% of U.S. retail motor-oil sales and 15% of the quick oil-change market. The Pennzoil restructuring, which has been expected, will leave the Houston outfit as an oil and gas exploration and production company.

REACH OUT AND CRASH SOMEONE

A CRITICAL AT&T DATA NETWORK crashed on Apr. 13 and wiped out the ability of thou-

HEADLINER: MICHAEL OVITZ

A NEW THEATER OF OPERATIONS

He used to look for value in directors and actors. Now, onetime superagent Michael Ovitz sees value in real estate. That's

a key reason Ovitz took control of Livent Inc., a troubled theatrical production company that also owns theaters in six cities, including the lavish new Ford Center on New York's Great White Way, where the hit *Ragtime* opened in January. Ovitz controls the company, after paying \$20 million for a 12% stake on Apr. 13 and installing investment banker Roy Furman to run the company that has been struggling

since its initial smash with the revival of *Show Boat*.

The Livent deal is just the latest Ovitz move

into real estate, fol-

lowing a recent joint venture

with land developer Glimcher

Realty Trust to

build entertainment-themed

shopping malls.

And there might yet be another real estate play

in Ovitz's future: For months, he has been trying

to put together a group to build a football stadium in

Los Angeles in hopes of luring a National Football

League franchise back to the football-barren city.

By Ronald Grove in Los Angeles



sands of corporate customers to send and receive data. The "frame relay" network failed when two Cisco Systems switches, which direct data traffic, stopped sharing data accurately and outages spread throughout the country. By the next afternoon, AT&T had succeeded in restoring full service across the entire country. Still, CEO Michael Armstrong pledged not to charge any companies for any frame relay service until the company eliminated the chance that similar problems could occur in the future.

CENDANT'S STAR SURE ISN'T RISING

DEALMAKER HENRY SILVERMAN may have gotten less than he bargained for. On Apr. 15, Cendant, created last year through the merger of Silverman's franchise giant HFS and direct marketer CUC International,

announced that it had uncovered potential accounting irregularities in certain former CUC business units. The bottom line: Cendant's 1997 net income is expected to be reduced by as much as \$15 million. Silverman said in a prepared statement: "We're outraged by the actions of a small number of former CUC employees who betrayed the trust placed in them by the company and our fellow shareholders."

ET CETERA...

- Thomas Evans, publisher of *U.S. News & World Report*, was named CEO of GeoCities.
- Justice's case against the Lockheed-Northrop merger will be heard in September.
- Representative Lee Hamilton (D-Ind.) called for easing the trade ban on Iran.
- Budget Director Frank Rains returns to Fannie Mae as its CEO.

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EDITED BY OWEN ULLMANN

THE FOLLY OF MAKING CLINTON'S CHARACTER AN ISSUE IN NOVEMBER

With Bill Clinton boasting a 70% job-approval rating despite Paula, Monica, and Kathleen, you'd think Republicans would give up trying to make his character issue. Nah. GOP leaders are convinced that carping about the House sleaze can be a winner in the November elections if they just give it time. "That fish has got to be out for a while before the American people see how rotten it is," says National Republican Congressional Committee chairman John Linder (R-Ga.).

House Speaker Newt Gingrich (R-Ga.) and other GOP leaders hold out little hope that Independent Counsel Kenneth W. Starr will give them enough ammunition to launch impeachment proceedings. But they relish the prospect of weeks of hearings that would air White House dirty laundry and, they pray, trigger a wave of public revulsion. Trouble is, the Clinton strategy could backfire, jeopardizing the GOP's slender hold on the House.

Lost Democrats, and even some Republicans, believe there would be plenty of public rage—but it would be directed at Clinton's mentors. "The more they spend their time talking about impeachment and Monica Lewinsky, the more they're telling the American people, 'We don't care about what you care about,'" says Democratic pollster Mark Mellman.

TA PARTY. Such talk worries some senior Republicans. They recall how Senate Banking Committee chairman Alfonse M. D'Amato (R-N.Y.) shot himself in the foot by going after the President and Hillary Rodham Clinton during hostile Whitewater hearings in 1996. "Republicans in a bind," concedes a party consultant. "Our base hates Clinton. But to appeal to the middle, we can't appear too partisan." The pragmatists' strategy: Let the press harp on Clinton scandals while Republicans stick to issues such as tax and Social Security reform.

For now, however, Clinton bashers are prevailing. GOP pollster Frank Luntz is egging them on, arguing that Clinton's popularity is broad but thin. "People almost insist on saying they like him even though they really don't like him," Luntz says. "He has the most defensive kind of popularity that I've ever seen in politics." Luntz's only caveat: Avoid impeachment talk, which voters view as reckless.

But instead of acting circumspect, many Republicans are throwing a Clinton piñata party. Senator John Ashcroft (R-Mo.), a White House aspirant with strong

Christian Right support, has labeled the President a sexual predator. House Majority Leader Richard K. Armey (R-Tex.) says Clinton should resign if the sex-and-coverup allegations are true. And some GOP candidates are already running TV spots that tie their Democratic foes to "Clinton sleaze."

SHOW TRIALS. The trick, the partisans contend, is to keep the attacks focused on Clinton's legal missteps—not his sex life. Emboldened by an MSNBC poll in which just 27% of respondents thought Armey had gone too far in blasting the President, the House plans to hold hearings on an array of alleged scandals. Among the possibilities: the White House "enemies list" and the Teamsters-Democratic Party campaign-cash connection.

These show trials will surely be boffo with the GOP faithful. But most voters seem willing to overlook Clinton's foibles as long as the economy keeps putting extra cash in their pockets. "In '96, Democrats morphed Republican candidates into Newt Gingrich, and it didn't work," says a senior GOP strategist. "If Republicans try this with Clinton, the result is likely to be the same." Or worse. If Republicans appear too mean-spirited, their desire to make Clinton an ex-President could make Gingrich an ex-Speaker instead.

By Richard S. Dunham



MONICA: A trap for the GOP?

CAPITAL WRAPUP

GIULIANI'S RUMINATIONS

Is New York Mayor Rudy Giuliani seeking higher office? The maverick republican is doing lots of national travel and has plenty of campaign cash. Even GOP conservatives are heaping his praises. One reason: Party strategists hope to entice Giuliani to challenge Senator Daniel P. Moynihan in 2000. Polls show that the popular mayor is the only Republican who could beat the veteran Democrat. A source close to Giuliani says that Hizzoner doesn't want to be just

one of 100 senators. He prefers an executive job, like governor (in 2002) or maybe even President (in 2004).

LINKING TOBACCO AND DRUGS

► House GOP leaders may tie tobacco legislation to the White House covets to new drug-enforcement measures. The goal: force President Clinton to adopt stiffer penalties against narcotics traffickers. The idea is to highlight Clinton's weak campaign against teen drug use. But the plan faces resistance in the Senate, which wants to stay focused on teen smoking.

DIAL 'C' FOR CONGRESS

► Baby Bells may soon get a hand from Capitol Hill in their thus far unsuccessful drive to enter the long-distance business. Senate Commerce Committee Chairman John McCain (R-Ariz.) plans to introduce a bill in late April clarifying the obstacles the Bells must surmount before they get the go-ahead. And the Senate Judiciary Committee is circulating a draft proposal that lets the Bells enter long-distance immediately if they split into wholesale and retail divisions.

“**W**hat a superb performance,”

gushed the woman when the recital was over.

“I’d give half my life to be able to play like that.”

“Madam,” responded the pianist with a little bow,

“that is exactly what it took.”



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CHROME, SWEET CHROME

A restless Japanese designer finds his dream job at Chrysler

Osamu Shikado's pulse raced as he entered the suburban Detroit warehouse on a bitter-cold New Year's morning. Inside, under a canvas tarpaulin, was Shikado's creation: a \$1 million Chrysler concept car called the Chronos. Designed by Shikado and built in record time, the Chronos sat hidden, awaiting the opening of the North American International Auto Show. But Shikado was itching to get a glimpse of his baby. When the tarp came off, the sight took his breath away. "It was my sketch come to life," he says.

Three days later, the Chronos was the talk of the auto show. As flashbulbs popped around him, Shikado knew he had hit a home run. The sleek, silver Chronos was the latest in a series of powerful, sexy concept cars, such as the Dodge Viper and Plymouth Prowler, from Chrysler Corp. And for Shikado, 43, who left his native Japan in 1994, its launch was the culmination of a personal odyssey. No designer had ever abandoned a career at Toyota Motor Corp. to emerge as a star in the U.S.

It's a high-stakes tale played out in a hypercompetitive arena. Shikado worked 14 years at Toyota on some of the world's best-selling cars, rising to become an assistant chief designer. But he had a burning ambition to break free of the bland Camry and Corolla and Toyota's bureaucracy. Frustrated and ready to gamble

on his talent, Shikado quit his \$80,000-a-year job in 1993. "Life is just one time," he says. "If I have a choice between something that's boring and something that's risky, I choose the risk."

His quest led him to Chrysler, home of one of the industry's most daring design teams. There, in the top-secret studios of the Chrysler Tech Center in Auburn Hills, Mich., Shikado has made his mark. Soft-spoken and conservatively dressed, he doesn't look like a maverick. But his calm exterior masks a fierce desire to create and compete.

SLIM CHANCE. When Shikado applied for a job at Chrysler in 1994, his future didn't look promising. After leaving Toyota, he first sought work in Europe, where the industry was in a slump: BMW, Volkswagen, and four Italian design studios turned him down. Unemployed and the father of two young children, Shikado was "deeply depressed." Since he viewed General Motors Corp. and Ford Motor Co. as every bit as conservative as Toyota, "Chrysler," he



was convinced, "was my last chance."

And it was a slim one. The carmaker usually hired designers fresh out of college. But Shikado's intellect and his determination to grow so intrigued Chrysler's execs, they hired him on the spot. "What he was doing was monumental," says Neil Walling, head of exterior design. "The fact that he gave up a job at Toyota showed an incredible dedication to design."

Shikado, in fact, has always followed his passion. As a boy growing up in Osaka, he adored animated Disney films and spent hours sketching characters from *Bambi* and *Peter Pan*. As he grew up, Shikado's devotion to drawing only intensified, much to the disapproval of

INSPIRATION

The Chronos (left) Shikado's winning concept car, drew on photos of the '53 Chrysler D'Elegance (above)





OSAMU SHIKADO

BORN

Apr. 14, 1955, in Osaka.

EDUCATION

Kyoto City University of Arts.
Graduated 1979.

CAREER

1979-93 Toyota team designer on the Corolla and Camry sedans. In 1985, studied design at Art Center College of Design in Pasadena, Calif. Promoted Toyota's assistant chief designer in 1989.

1994-PRESENT At Chrysler, helped design a trailer for the Plymouth Prowler. Worked on design team for the 1999 Neon subcompact. Won an internal competition in 1997 to design the Chrysler Chronos luxury concept car. Promoted to senior designer in 1997.

PERSONAL

Married, with a son and daughter.

WHY HE CAME TO THE U.S.

"Life is just one time. If I have a choice between something that's boring and something that's risky, I choose the risk."

had won kudos for the 1998 Chrysler Concorde sedan. But Hall knew little about his Japanese rival. "He seemed very quiet and technically proficient, not the kind of guy to be blowing his own horn," Hall says.

Hall and Shikado faced off around a single large block of clay—about half the size of a full-scale car—each executing his design on opposite halves of the block. Directing trained modelers on every little detail, Shikado's dream began to come alive. Occasionally glancing at each other's work, the two rarely spoke. Hall's design was a beauty. Whenever Shikado's confidence flagged, he just thought back to the photo of the D'Elegance and pushed on.

MASS MODELS. D-day came on Mar. 7. Gale, along with Chrysler Vice-Chairman Robert A. Lutz and other execs, slowly circled the two-sided clay model. Gale was instantly taken by Shikado's classy entry. "Osamu had obviously listened very carefully to the assignment," Gale recalls. Shikado, meantime, was a bundle of nerves as he waited out the decision over lunch. But when he returned to the office, Shikado got the good news. Overwhelmed with emotion, all he could think about was his father, who had died two months earlier in Japan. If only his father could have shared the moment, Shikado thought.

Even if the Chronos is never produced, it "will have a profound effect on what we do," says Gale, who envisions the Chronos' retro look making its way into mass-produced models. More important for Shikado, the Chronos means vindication and a bright future. At Toyota, "he was not so high-ranking," says Tetsuo Kitagawa, a Toyota spokesman. Now, Shikado has already been put in charge of a new concept design that will debut at the 1999 Detroit auto show.

Shikado says he's here to stay. His family has settled into the sizable Japanese community that has grown up around the Detroit auto industry. (Shikado declines to reveal the names of his wife, son, and daughter.) His son, 10, even wears a Detroit Red Wings jersey in street roller-hockey games.

In time-honored auto-design tradition, Shikado isn't breathing a word about his current project, except to say he couldn't be happier with his assignment. "Every time I present some sketches, [my boss] encourages me to be bolder," he says as he runs a hand across the broad hood of the Chronos. For Osamu Shikado, that shouldn't be a problem.

By Bill Vlasic in Detroit, with Emily Thornton in Tokyo

father, a stern high school biology teacher. Even his teachers urged him "stop scribbling" and become an engineer. Shikado wasn't deterred. He entered the Kyoto City University of Arts in 1975. Upon graduating in 1979, Shikado landed a design job at Toyota.

ARCHIVES. It wasn't until he got to Chrysler, though, that he could really spread his wings. Shikado immediately moved into his work. But only a handful of designers ever get a chance to design a concept car—much less a new model from Japan. Shikado had done well in his first 2½ years, though he was hardly a star. His biggest accomplishment was working on the team designing the new Neon subcompact. But when his team was chosen to compete for a shot at designing a superluxury car, Shikado made the most of it.

It was an assignment 180 degrees from the four-door sedans that Shikado worked on for years at Toyota. "The task was to capture the essence of a classic Chrysler car," says Thomas C. Hall, executive vice-president for product strategy. Two managers and four designers, including Shikado, would work alone for two weeks to produce

their sketches. Two finalists would then be chosen by Gale. Shikado's competitive fires burned as he contemplated the opportunity. "I wanted nothing but to win this project," he recalls.

The others went directly to their sketch pads, but Shikado's love of old cars led him to the tech center's photo archives for inspiration. After a few hours of research, one model stood out: the 1953 D'Elegance. Its big wheels, massive grille, and rakish roof embodied the prosperity of the 1950s. But two weeks was hardly enough time to translate the classic into a car for the '90s. So Shikado worked evenings and weekends. Happy to put in the extra hours, he let his imagination run wild as his embryonic car took shape.

When the two weeks were up, Gale eliminated four of the six competing designs. Shikado's and another by Mark Hall, one of the company's hottest stars, survived the cut. Now, the pressure was really on. Shikado and Hall had just three weeks to turn their designs into 6-foot-long clay models for final review. Shikado faced keen competition in Hall, a former jewelry designer and sculptor who had joined Chrysler in 1984 and

WORK & FAMILY

PARENTS OF THE WORLD, UNITE

A national organization aims to mobilize moms and dads

Millions of Americans share common ground rooted in a singular and life-changing experience. Chances are good, in fact, that you're one of them. But this massive minority has no real political voice and no legislative agenda. Can they unite?

Economist Sylvia Ann Hewlett thinks it's about time they did. Her fledgling National Parents Assn. (NPA) seeks to organize the nation's 62 million parents of children under the age of 18 who, she says, face stressful lives with little cultural or social support from business and government. "Parenting is the ultimate nonmarket activity," she observes. "We've had a hard time giving it stature and standing."

CONSPIRACY. In their new book, *The War Against Parents* (Houghton Mifflin), Hewlett and Cornel West, professor of philosophy of religion and member of the African-American studies department at Harvard University, describe the ways in which they believe parents are conspired against. It starts with the time and money crunch wrought by inflexible work hours, insufficient and unpaid family leave, a marriage tax penalty, and for some, low wages. It extends deep into popular culture, which often denigrates parents and parenting in vapid sitcoms, among other arenas. The role of fathers has been especially underrated and misunderstood, they contend.

Recalling the 1944 GI Bill of Rights, which helped launch a period of postwar growth by giving returning military veterans financial and educational aid, Hewlett and West propose a "parents' bill of rights" (table, page 60). It would provide generous allowances for families—from 24-week paid parenting leaves to subsidies for low-wage workers. They urge a lengthening of the



school day and the school year to better reflect a changing society in which the majority of families are dual earners.

To help make it all happen, Hewlett and West have created the national organization with nearly 9,000 members in six states. Working with school boards and businesses and at the local, state, and federal levels, the NPA will mobilize parents across the political and racial spectrum and eventually do for parents what the American Association of Retired Persons has done for seniors, Hewlett and West hope. The NPA, headquartered in New York City, has membership dues of \$25 a year.

Hewlett, 51, gave birth to her fourth child just over a year ago, and also has a stepchild. West, 45, has a 20-year-old son. They emphasize that they don't

want parents to be viewed as yet another interest group. "Nonparents have a stake in all citizens of the future ending up in good shape," Hewlett says. Parents invest upwards of \$150,000 to raise a child, she notes, but many of that child's contributions as an adult may accrue to society at large.

Hewlett's and West's concerns are not unfamiliar, of course: For all the lack of explicit representation, parents have a host of surrogate advocates. Con-

servative politicians and legislators, recently joined by politicians of nearly all stripes, have long embraced the fuzzy cause of family values. Women's groups, children's advocates, and research organizations have long fashioned agendas to help children and families. The National Partnership for Women & Families—formerly the Women's Legal Defense Fund—did pioneering work 14 years ago

THE NEXT AARP?

The National Parents Assn.'s Sylvia Ann Hewlett and Cornel West could wield enormous clout

to promote family-leave legislation that finally became law in 1993; it now is working to expand coverage to smaller companies and helping some states find new ways to fund family leave. The Children's Defense Fund is pushing an initiative to make child care more affordable and more widely available.

Such groups believe a parents' movement would only complement their efforts. "Rarely before in American history have we expected parents to do this challenging job totally on their own as a private matter," observes Wend Lazarus, director of the Children's Partnership, a Santa Monica (Calif.) nonprofit, nonpartisan group that researches children's issues. "We need to once again establish that parents are doing something that is of civic value."

"LIVING WAGE." Numerous research groups churn out ever more compelling data confirming the demands of parenthood in the two-income-family era. On Apr. 15, the Work & Families Institute released a major study on the changing workforce in America. Among its key findings: Employed married fathers spend more time with their children

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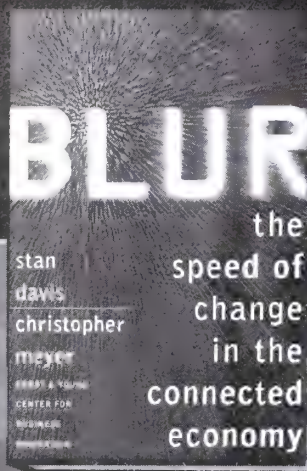
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on page 130

Social Issues

PARENTS' BILL OF RIGHTS

An agenda for reform from Sylvia Ann Hewlett and Cornel West

TIME-BIND RELIEF Provide paid parenting leave, flexible work-places, part-time career ladders, and tax breaks for at-home parents.

ECONOMIC SECURITY Guarantee parents a living wage, introduce a family allowance for families with children under six, eliminate sales tax on children's necessities such as diapers and car seats.

LEGAL STRUCTURES Promote premarital counseling and make it harder to divorce. Restructure welfare to favor two-parent families.

SUPPORTIVE ENVIRONMENT Create a lobbying group to represent parents. Extend the school day and year, and increase spending on early childhood education.

DATA: SYLVIA ANN HEWLETT, CORNEL WEST, NATIONAL PARENTING ASSN.

than fathers did 20 years ago, while mothers spend about the same amount—but 70% of all parents feel they do not have enough time with their children.

Hewlett and West's proposals are ambitious. Providing wage subsidies to guarantee all workers a "living wage" of \$7.00 or so an hour—a proposal based on work by Columbia University economist Edmund Phelps—would cost \$10 billion a year initially. Representative Lynn Woolsey (D-Calif.), who hopes to introduce an "income-protected leave bill at the beginning of the next session of Congress, concedes that mandating paid time off for new parents will be a tough battle.

The authors know that their proposals are expensive. But their parents' bill of rights is, they say, a starting point, something to be refined and debated as parents around the country unite to make schools, communities, businesses, and government more responsive. Hewlett and West are on a mission—a mission to give parents voice. Given full expression, that voice could one day prove the loudest and most powerful in the nation.

By Karen Pennar in New York



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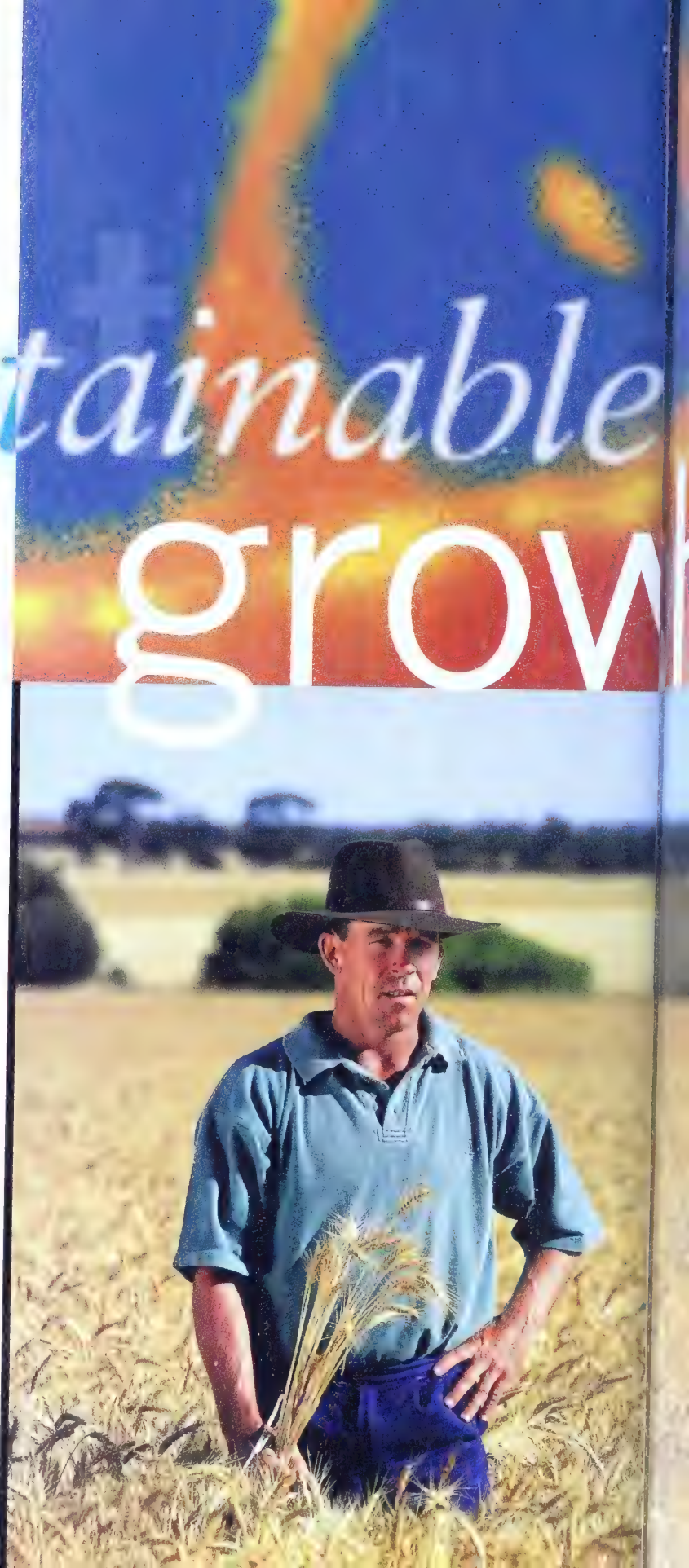
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RESEARCH

STARVING TUMORS TO DEATH

A new approach cuts off cancer's blood supply

Medical researchers searching for a "magic bullet" that could treat cancer without poisoning the patient may be on to something. Instead of using chemotherapy or radiation to attack the tumor, they're trying to starve it to death. More than a dozen drugs currently under development have shown remarkable success in treating breast, brain, and lung cancers in mice by blocking blood vessel growth to tumors—essentially cutting off their life-support system. Even more exciting, some of these compounds have eradicated cancer in mice altogether.

This elegantly simple approach is one of the hottest areas in cancer research, with some 25 pharmaceutical and biotechnology companies around the world working on it. Outfits ranging from drug giants such as SmithKline Beecham, Merck, and Novartis to startups Entremed, SUGEN, and British Biotech are all testing compounds that block a process called angiogenesis, the growth of new blood vessels. These drugs could address a much broader range of cancers than most existing drugs, which are usually highly toxic and work only against one or two types of cancer. The new drugs—called angiogenesis inhibitors—block the chemical signals that tumors send out to attract new blood vessels. Because the signals are the same across a broad range of cancers, the drugs should stop almost any kind of cancer.

MEGAMARKET. With more than 1 million new cancer cases diagnosed each year in the U.S., the market for angiogenesis inhibitors could be enormous. The compounds are also being tested against macular degeneration, a common cause of blindness in the aged that occurs when blood vessels grow over the cornea, and which afflicts an estimated 13 million Americans. Wall Street analysts predict that an angiogenesis inhibitor could be the first cancer drug to reach blockbuster status, with annual sales exceeding \$1 billion.

At least 9 of the 12 or so compounds found to inhibit the growth of new blood

vessels to cancer tumors are already in clinical trials. They include the controversial drug thalidomide, marketed as a sedative in the 1960s before it was found to cause horrific birth defects when taken by pregnant women. Researchers discovered in 1992 that thalidomide blocks blood vessel formation, which is why it caused birth defects in the first place—it cut off blood vessel formation in the fetus. Now, in clinical trials being conducted by the National Cancer Institute, the drug is showing promise against the toughest tumors.

To avoid the problems of thalidomide and other first-generation compounds, the new group of angiogenesis inhibitors targets blood vessel growth more specifically, offering the promise of powerful cancer drugs virtually free of toxic side effects. A recent Lehman Brothers Inc. study that examined a variety of new cancer treatments concluded that angiogenesis inhibitors are the ones likely to "provide the foundation for cancer therapy in the future."

The explosion of interest in these drugs was evident at a meeting of the American Association for Cancer Research in New Orleans in March, where researchers presented some 50 papers on the subject, up from a handful a year earlier. Among the most startling was a report by Dr. Erkki Ruoslahti, president of the Burnham Institute, a nonprofit research center in La Jolla, Calif. He described a "one-two punch" that knocked out cancer in mice permanently. Ruoslahti's team combined doxorubicin, a widely used chemotherapy drug, with an angiogenesis inhibitor called tumor homing peptide (THP).

The mice implanted with human breast cancer cells that received Ruoslahti's compound, called THP-dox, showed no recurrence of cancer during

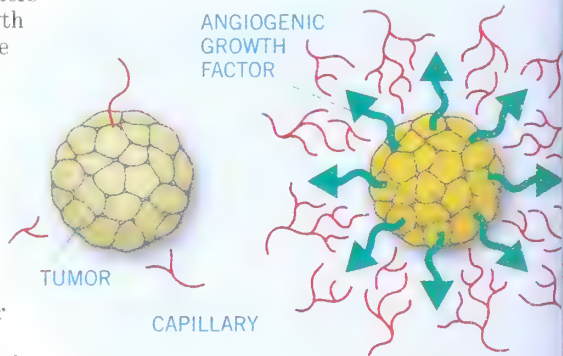
their lifetimes, while the mice receiving only doxorubicin died either of drug poisoning or tumors that developed drug resistance. "This is one of the most exciting pieces of work I've seen recently," says Donald S. Coffey, professor of oncology research at Johns Hopkins University School of Medicine. "He really seems to have finally beaten the resistance mechanism." THP-dox has been licensed to ILEX Oncology Inc., which is aiming for clinical trials in two years.

Despite these early successes, researchers have a long way to go from mouse to human, cautions Dr. James Pluda, senior clinical investigator of the National Cancer Institute's investigational drug branch. "The field of oncology is littered with the bodies of agents that were the next magic bullet," he says. But, he adds, "I think this form of therapy may be an important weapon in our arsenal against cancer."

Dr. Judah Folkman of Children's Hospital, Boston, first theorized that cancer tumors depend on angiogenesis 30 years

HOW IT WORKS

Compounds under development attack cancer support system rather than the tumors themselves



1 TUMOR cannot expand because the outer cells are not in contact with blood vessels

2 Tumor releases signals called ANGIOGENIC FACTORS that induce new blood vessel growth

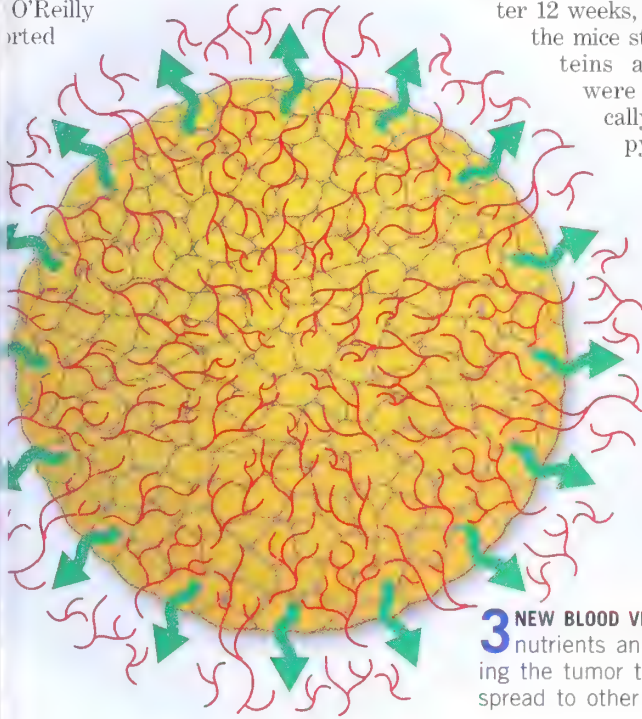
ago. But it is only in the last five years that molecular biologists have been able to isolate the cell mechanisms that trigger the process.

Blood vessels normally have only one big growth spurt, in the fetus. After birth, there are three instances in a healthy person when new capillaries sprout—menstruation, pregnancy, and wound healing. The big exception is cancer. When rogue cancer cells first emerge in the body, they rapidly divide and form a tumor about the size of a pea—too far away from the surface

existing capillary to receive nourishment. This tumor can remain dormant for several years. But at some point it starts sending chemical signals to the endothelial cells that make up blood vessels. In response, new capillaries are formed that reach out to the tumor, carrying nutrients and oxygen. The tumor starts expanding, sending out cells along the capillaries until it spreads throughout the body.

SWITCH. Sometimes, however, that tumor also sends out signals that suppress the formation of secondary tumors elsewhere in the body. In that case, the tumor applies chemical "brakes" that put a stop to capillary growth. Folkman and his colleague Michael O'Reilly have isolated two of these primary tumor brakes, proteins called angiostatin and endostatin. Cancer experts say they may be the most powerful angiogenesis inhibitors

as of November. O'Reilly reported



Co., that will be available in much larger quantities. Kim Lee Sim, senior director of molecular biology at EntrezMed, says the recombinant version of angiostatin reduced the number of melanoma tumors in mice by 60% to 80% after 11 days of treatment, and those that remained were tiny. "We've effectively turned off a switch that the body turned on," says EntrezMed Chairman John W. Holaday.

To keep that switch off permanently, scientists from Genetix Pharmaceuticals Inc. in Cambridge, Mass., introduced the genes for endostatin and angiostatin into the bone marrow of tumor-infected mice. After 12 weeks, they reported that the mice still carried the proteins and their tumors were reduced dramatically. The gene therapy approach, says

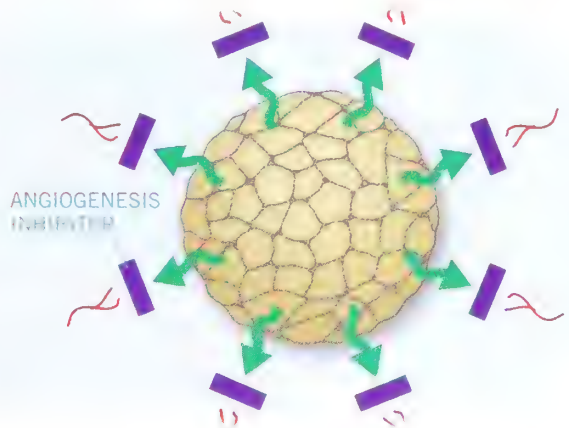
These remedies may address a wide range of cancers with little or no toxic side effects

high potency against human stomach tumors that had been implanted in mice. And a team from Monsanto Co. reported on yet another compound as safe and effective against solid tumors in mice.

There were also reports on compounds derived from shark cartilage, a cancer folk remedy long dismissed as ineffective by medical experts. But researchers have found some proteins in shark cartilage that do block blood vessel formation.

Bioengineered versions include Neovastat, made by Aeterna Laboratories of Canada; squalamine from Magainin Pharmaceuticals in Plymouth Meeting, Pa.; and Troponin I, from Boston Life Sciences in Boston. All have dramatically reduced the size of tumors in mice without toxic side effects.

A lot of work still needs to be done before the newest angiogenesis inhibitors are proven in humans. Most of them are expected to enter clinical trials later this



3 NEW BLOOD VESSELS deliver nutrients and oxygen, allowing the tumor to grow and spread to other organs

4 ANGIOGENESIS INHIBITORS block growth signals and kill the new blood vessels, causing the tumor to shrink

he could eliminate some of the factors altogether in mice by using endostatin and angiostatin in combination. He had only minute amounts of the proteins, which he had painstakingly isolated from mouse urine. Baltimore (Md.)-based EntrezMed Inc., which underwrites Folkman's research, has taken a big step toward commercialization, however. The company announced at the recent cancer research meeting that it had successfully produced a bioengineered version of angiostatin, licensed to Bristol-Myers Squibb

Genetix scientist Dr. Robert Pawliuk, empowers the body to make its own cancer-fighting proteins, eliminating the need for daily injections.

There are other angiogenesis inhibitors under development and a steady stream of promising new studies. At the New Orleans meeting, researchers from TAP Pharmaceuticals of Japan reported that their TNP-470 compound prevented the spread of lung and skin cancers in mice during 20 days of treatment. Japanese researchers demonstrated that another inhibitor showed

year, and it will be four or five more years before they could win approval—if the trials are successful. But researchers say the angiogenesis inhibitors have already had a tremendous impact on the way laboratories are thinking about cancer. "There are two ways to make an organism extinct. Knock each one out individually or knock out its habitat," says Coffey. "The second way is a lot more effective." Someday, researchers hope, that change in thinking will lead to a dramatic change in treatment.

By Catherine Arnst in New Orleans

ANALYZING INFORMATION



[WHAT THE HIVE]

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FOR A HEALTHY ART, PIG OUT FOLIC ACID

AN. 1, THE FOOD & DRUG Administration dictated that cereals, breads, and pasta should contain at least 140 micrograms of folic acid per serving to protect against birth defects. It was a good idea, except for one thing: the level of folic acid may be too low. The consumption of folic acid, found in grains and in green vegetables such as spinach, has been linked to lower rates of spina bifida and other birth defects. An 11-year study in the *New England Journal of Medicine* reported that folic acid also lowered blood levels



FORTIFIED: A daily 400-mcg dose may do the trick

of homocysteine, a substance linked to heart disease. But the study, done at the Oregon Regional Primate Research Center, found that homocysteine levels fell only in those subjects who consumed 400 micrograms of folic acid a day in their fortified cereal. That is double what most Americans actually get. *Catherine Arnst*

BETTER WAY TO BUILD A BATTERY

STEAD OF SCREENING thousands of chemical compounds at random to find drugs, pharmaceutical companies often use a technique called rational drug design to create them from scratch. At the Massachusetts Institute of Technology, materials scientists are taking the same tack.

In the Apr. 16 issue of *Nature*, a group of MIT professors describe the invention of a lightweight and inexpensive cathode for lithium-ion batteries, which could replace a pricey lithium-cobalt compound that's widely used today. Instead of testing thousands of possible replacements, the MIT team calculated the optimum characteristics for the cathode—one of two electrodes in a battery that combine to create a current. Then the scientists concocted a cobalt-alumin-

um mixture to fit the bill.

The professors have licensed the new cathode to Pacific Lithium Ltd., an Auckland, New Zealand, supplier of high-grade lithium. The company plans to market the cathode in late 1998. And it could reduce battery prices by 25%, says Pacific Lithium CEO Robin T. Johannink. But that's just for starters. The MIT team has licensed Pacific Lithium a second cathode design, for which patents are pending. Gerbrand Ceder, principal author of the *Nature* paper, won't identify the second compound. But he says it will bring further reductions in battery weight and price. Next year, the same scientists may have an even bigger announcement. They're working on a whole new concept for light, flexible lithium batteries that don't require any liquid electrolytes. □

BIO WARFARE'S NEW RECRUITS

VACCINES COULD PROTECT SOLDIERS AGAINST INSIDIOUSLY altered strains of anthrax and other microbes. But the vaccines must be deployed quickly. With today's tools, it could take scientists months to culture some virulent new strain, choose a protein target, purify it, and incorporate it into a vaccine.

Help in speeding that process may come from tiny Siga Pharmaceuticals Inc. in New York City, which recently received an \$800,000 grant from the Defense Advanced Research Projects Agency for vaccine development. Siga's technique involves attaching foreign proteins such as antigens and antitoxins to harmless bacteria that normally inhabit mucous membranes of the mouth and nasal passage—the primary gateways to infection.

This method of attaching proteins is the product of 30 years of research at Rockefeller University by Siga's co-founder Vincent A. Fischetti—head of Rockefeller's bacterial pathogenesis lab—and by his partner, Oregon State University biologist Dennis E. Hruby.



GAS DRILL: Vaccines can take months to make

Ultimately, within a week of identifying a pathogen on a battlefield, scientists should be able to select an appropriate host bacterium in the nose or mouth and reprogram its genes. The host could then secrete an antigen in the soldier's tissues to prompt an immune response in case of a viral attack. Or the bugs could be forced to secrete enzymes that would break down botulin or other toxins. □

THE GREENING OF NEW YORK CITY'S YELLOW CABS

TAXIS JUST PASSED A MILESTONE in the war against foul air: For the first time, a big taxi fleet has switched from gasoline to 100% natural gas. In April, Ford Motor Co. sold 100 special Crown Victoria cabs to Winner's Garage in New York City.

New York has 12,000 cabs, more than any other U.S. city, and they produce up to 25% of the city's pollution. So Ford chose New York as the launchpad for a campaign to sell its NGV (natural gas vehicle) Crown Victorias. Ford

and government planners figure that if all the city's cabs switched to gas, 2,600 tons of air pollutants would be eliminated a year. And judging from the performance of NGV fleets run by utilities, airports, and the U.S. Postal Service, the switch would also trim fuel costs by 20% or more.

Before April, only a handful of NGV cabs had been sold—perhaps because special fuel tanks and other parts typically add \$10,000 to the sticker price. But with beefed-up incentives from industry and government agencies, more taxi fleets will make the switch, says Brooklyn Union Gas Co., which supplies the fuel. *Otis Port*

A black and white photograph of the Titanic ship, showing the upper decks and the iconic funnels. The ship is viewed from a low angle, emphasizing its massive scale. The word "TITANIC" is faintly visible on the side of the hull.

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In Box page 2

Get Smart Taxes, pensions, CEO archetypes, schmoozing, and more

Management page 4

Basis for Comparison Think you know how your company's doing? Benchmarking can offer surprises



Companies page 8

Movie Men Sprucing up Mexican cinemas started out as a class project for three Harvard men—and turned into a career

Marketing page 12

Package Deal How tiny mountainhead squared off against big wals in the crowded designer-water market



Technology page 14

To Buy Or... Is leasing a state-of-the-art PC really a better deal than owning? The short answer: It depends

Personal Business page 20

Breaking the Code What do all those changes in the tax code mean? Some of the most ballyhooed new breaks account for little. On the other hand, you may find an unexpected savings or two



Roundtable page 26

Family Ties Career and family never mix easily. When a spouse owns a business, problems multiply. Azriela Jaffe has made a business of advising on how to strike a balance

Buyer's Guide page 28

Don't Hold the Phone A \$100 headset can end head and shoulder strain. But buyer beware: All headsets are not created equal



Downtime page 34

Heard Any Good Books? Pop a business best-seller into the tape deck—and turn the commute into a mini-course



IN BOX

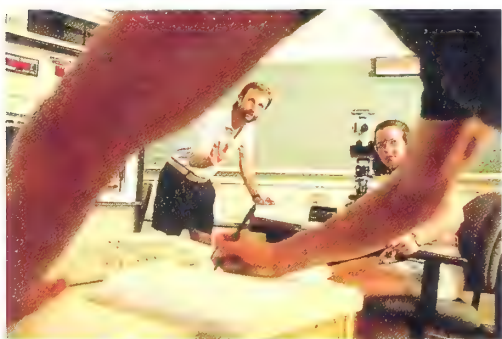
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UPDIKE

UNCLE SAM WANTS YOU—TO HAVE A PLAN

Only 20% of companies with fewer than 100 employees offer retirement plans—and that's something Washington wants to change. Two new legislative proposals would give small-businesses tax credits of up to \$4,000 over three years to help set up a plan and educate employees about it. Meanwhile, on Mar. 23, the IRS eased rules in its "voluntary correction" programs, which allow companies to find and fix administrative mistakes that would otherwise disqualify their pension plans from tax bene-

fits. Previously, an employer who stepped forward could be liable for up to 40% of all the payroll tax on plan contributions. Now, such payments are limited to \$500 to \$4,000, depending on circumstances. Also, the time period for self-correction was doubled to two years. Visit www.benefitslink.com for easy-to-find info on pensions and other benefits.

BUSINESS' CLASS ACT



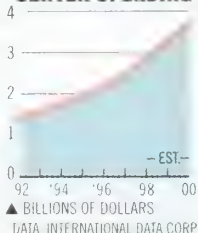
TRAINING PROGRAMS ARE WAY UP

Smart companies are fighting the labor squeeze by raising workers' skills, not just wages. A new Coopers & Lybrand survey of fast-growing companies finds more than half have launched new training initiatives in the past two years—42% with internal programs and 36% using outside courses. The federal government is encouraging the trend with tax incentives. Workers can receive up to \$5,250 in compensation, tax-free, for undergrad studies or graduate courses that are job-related. Last year's tax act extended the benefit to courses starting by June 1, 2000. Survey respondents cited a wide variety of educational needs. Problem-solving (31%) and computer and technical skills (21%) topped the list. Twelve percent say that even basic math and reading skills are wanting.

NETWORK NEWS

Even very small business is going high-tech with networks, according to International Data Corp. More than half of networked businesses with under 20 employees have servers. Such technology speeds Net connections and supports more sophisticated software without requiring a lot of tech staff. Rising spending (chart) by companies of fewer than 100 workers is due to falling prices and more Internet/Web use.

SMALL BIZ LAN AND SERVER SPENDING



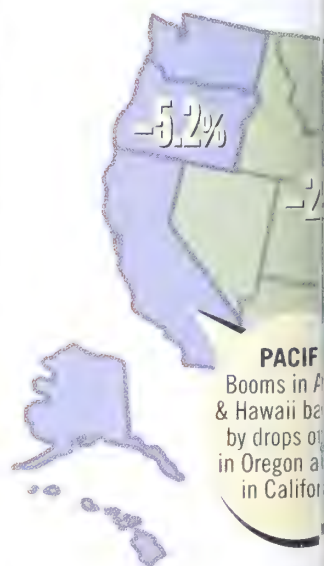
For more information on small-business LANs, visit BW Plus! at www.businessweek.com or AOL at keyword: BWEnterprise.



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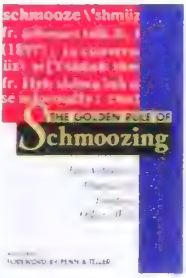


THE NUMBER OF SMALL BUSINESSES OFFERING

HEALTHCARE BENEFITS FELL 7% IN 1997, TO 39%,

RT OF THE SCHMOOZE

ne think it cheesy or sleazy, but median Aye Jaye says schmooz-just shows you care. Not ctly about busi-s, his good-hu-ed new book, *The ten Rule of moozing*, tells and why special tment of oth-employees, ts, friends, and ses—can pay dividends without costing much. (Sourcebooks, \$12.95: 432-7444)



l out that we were paying too quickly. Our cash flow l significantly.”
Runck, vice-president for finance Transport & Rigging Inc., on how ing helped his company (page 4)

Do CEOs improve with age or lose their edge? Both, according to Hagberg Consulting Group, an executive development firm that does most of its work in Silicon Valley. Hagberg reviewed the performance evaluations of 550 top executives done by both the executives themselves and their colleagues. CEOs under 35 years old don't prioritize well and forget details, the study claims, but they're also daring and decisive. Older CEOs are better listeners and planners, but not as persuasive. That's why venture capitalists often pair senior sages with young CEOs.

THE AGE-OLD QUALITIES OF CEOs

YOUNGER

- Energetic
- Daring
- Creative
- Impulsive
- Hard-driving
- Nonconformist
- Apprehensive

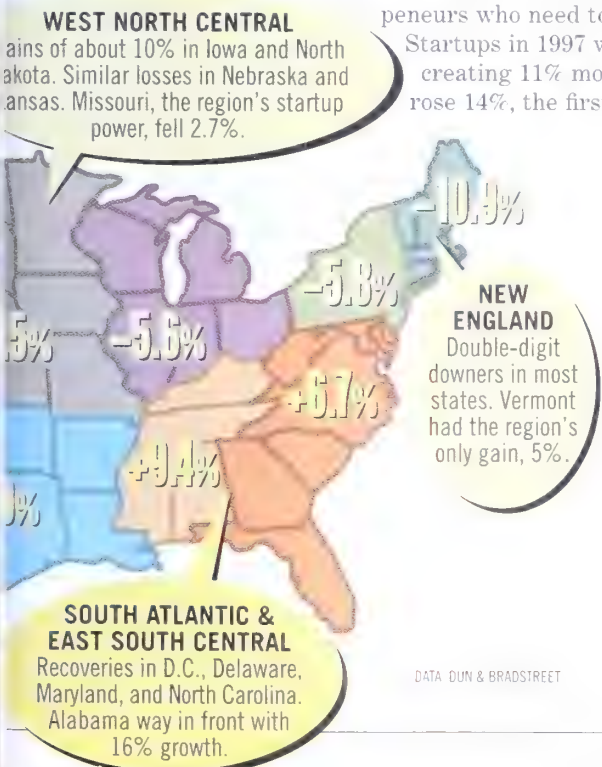
OLDER

- Open-minded
- Detail-oriented
- Organized
- Sensitive
- Even-tempered
- Trusting
- Delegating

DATA: HAGBERG CONSULTING GROUP

S ROSE AN AVERAGE 13%, SAYS A D&B POLL

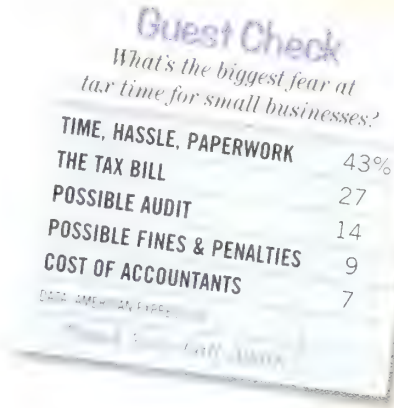
business starts in the U. S. fell 2.2% in 1997, Dun & Bradstreet Corp. data show. The early 1990s saw loads of laid-off workers go solo; now, a tight labor market encourages marginal entrepreneurs to stay on a payroll. Also, rising expenses squeeze margins—discouraging would-be entrepreneurs who need to break even quickly. Startups in 1997 were generally larger, creating 11% more jobs than '96. Failures rose 14%, the first uptick in three years.



FIE ON FILING

If you haven't filed your taxes yet, you're not alone—just in the minority. Some 14% of 303 small-business owners polled recently said they usually get extensions, and 7% don't start until a week before Apr. 15. Some of them may be the same ones who keep receipts in the proverbial shoebox (15%).

Most business owners are more organized, though. Roughly half start preparing three months ahead, and 25% allow at least a month. Three-quarters file receipts and use accountants. Only 10% use tax preparation software; 4% dump the job on a spouse.



BETTER YOUR BUSINESS: BENCHMARK IT

Measuring your company against others can spark changes that give you a leg up

Business owners like to think they know intuitively what's going right at their companies—and what's not. But Elfrena S. Foord, a financial adviser in Sacramento, wanted hard evidence. In her business, winning the client's trust is everything. She needed to know if she was getting it.

So the managers at Foord, Van Bruggen & Ebersole decided last year to check on what customers really thought about their service by doing some benchmarking—a process that measures a company against the standards and practices of other companies.

The results were surprising and sometimes humbling. While the firm got high marks for performance compared with its peers, a consultant's study concluded that the partners weren't meeting often enough with clients. "I also found out I wasn't as good a communicator as I thought I was," says Foord. She promptly enrolled in a four-weekend course. The upshot, says Foord, is that today business is up 10%, a rise she credits in part to the benchmarking study.

BEST PRACTICES. The use of benchmarking is growing quickly among small companies as it becomes easier to do, experts say. Huge amounts of data have become accessible, on software and through the Web, that allow owners to find out how rival companies are doing—and how they do it. Done properly, the process can improve customer satisfaction, identify industry breakthroughs, and spark changes that give a company new competitive advantages.

Benchmarking falls into two major categories. The first is a simple comparison of common financial measures—such as debt load and inventory levels—to the norms for a particular industry. But these ratios tell you only that something is wrong. Finding the problem and fixing it requires a second kind of benchmarking, a more qualitative but still systematic search to identify the best practices in your industry. Instead of merely asking: "How am I doing?" say advocates of this process,

you need to be constantly asking: "What can I do better?"

The financial snapshot is an important first step, though. The idea is to focus on key business ratios to see if you're way out of sync with similar companies. For example, if you're carrying more debt than most rivals, you might have trouble weathering a recession or price war.

STRATEGIES

Other criteria to focus on include inventory turnover, return on investment, selling, general and administrative expenses as a percentage of revenue, and liquidity measures, such as current and quick ratios, which tell you whether you have enough cash on hand to pay routine bills. "Often, businesses think their performance is pretty good and are shocked to s



they compare to others," says Daniel W. Bookhart, a benchmarking consultant in Chadds Ford, Pa. Rountree Transport & Rigging, a specialized long-distance trucking company based in Jacksonville, Fla. In 1990, Rountree used Dun & Bradstreet's BusinessScope database to see how its receivables and payable stacked up against its rivals. It discovered that receivables went uncollected for an average of 48 days, vs. an average 33 days for the industry. In effect, Rountree was giving its customers an interest-free loan.

ON THE BILLS. The problem, officially discovered, was that Rountree waited until they returned to the nearest terminal to turn in invoices. Now, invoices are turned in immediately after they get to the closest terminal. This simple change cut billing time in half, from 12 days to 6 days, and outstanding receivables dropped to 28.5 days, well below industry average.

We also found out that we were pay-



UPWARD PATH: Instead of merely asking: "How am I doing?" say advocates of this process, you need to be constantly asking: "What can I do better?"

ing bills too quickly," says Thomas D. Runck, vice-president for finance. Now, bills are paid five days before the due date, unless a discount is offered for early payment. "Our cash flow improved significantly," says Runck.

The real benefits of benchmarking come, though, from taking a more proactive approach. Instead of waiting for a problem to arise, avid benchmarkers make it part of their routine to seek out and measure the best practices in use elsewhere—and then shamelessly adopt those tactics as their own.

Unlike ratios, comparisons of business practices don't come neatly packaged in a database; someone has to go out and look for them. The search need not be limited to your rivals. You can compare processes within your own organization or among companies with similar processes, even when they're outside your industry. The inspiration might even come from best practices at a company that is completely different.

Popular targets for benchmarking include cycle time—how long it takes to do a job or launch new products—and asset management, which scrutinizes how equipment and people are employed. But customer satisfaction is the topic studied most often, and it's not just a matter of asking customers what they think. The trick is in how you ask it, as the Houstonian Hotel & Spa learned when it set out in 1990 to benchmark its customer service against its peers.

The idea was to identify problems from customer comments and then adopt the best practices to improve the Houston hotel's rating. It soon became apparent that the Houstonian's existing effort at benchmarking was part of the problem. The staff always left a

40-question comment card in each of the 300 rooms, but the response rate was a meager 2%—no more than par for the industry. "We only heard from those who were very dissatisfied or very satisfied," says Greg Clark, executive vice-president.

Clearly, the survey itself didn't measure up to best practices. The solution came not

from another hotel, but from a nearby auto dealership where a hotel manager was having his car serviced. The cashier handed him his bill and a comment card—with only four questions. Unlike Houstonian's exhaustive quiz, this one took only seconds to fill out.

START DIGGING. So, the Houstonian chopped up its survey into 10 different cards with four questions each and handed one card to customers at check-out. The result? Today's response rate has soared to 80%. The staff chimed in by proposing that suggestions from the cards should be circulated daily, instead of going to company headquarters. The payoff: Clark says customers who say they would choose the Houstonian again rose from 85% five years ago to 99% recently.

Sound like something you would like to try? There are two ways to go about it: You can do it yourself—providing you can spare the time. Or you can hire a consultant, providing you can afford the considerable fees.

First, decide what to benchmark by starting with a good internal financial analysis from a commercial database (table, page 6). Trade groups and government agencies also offer databases designed to help you compare financial performance and benefits against your peers.

Next, put together a benchmarking

team. To do it right, they will need to devote half a day each week for a couple of months. It won't work if the goals aren't specific, so choose no more than three topics to benchmark at once.

Then, start digging. "Ask yourself, where can I best learn the process I want to improve," says Fred D. Bowers, a consultant based in Acton,

Measuring Up

More than 80% of fast-growing small companies employ benchmarking to improve their performances. The most commonly used gauges:

INDUSTRY NORMS

34%

PRIMARY COMPETITOR

28%

INDUSTRY LEADER

25%

SIMILAR WORLD-CLASS FIRMS

18%

OTHER

5%

DATA: ERNST & YOUNG

Mass., who in 1990 created Digital Equipment Corp.'s benchmarking program.

You can arm your team with a host of data on benchmarking from the Web and your local library. A good place to start is the Benchmarking Exchange (www.benchnet.com), which helps companies share information from surveys, market studies, and lists of best-practice companies. Take a peek at rivals' Web sites. Business gumshoes who specialize in "competitive intelligence" often are amazed at the intimate data some companies choose to post.

Next, identify companies that may serve as benchmarking "partners"—companies with best practices that might teach you what they do. Network among customers, suppliers, and employees, and ask them who they think is best at the process you're trying to improve. Other sources to poll include chambers of commerce, small-business development centers, trade associations, industry experts who know of breakthrough practices, and companies that have won local and state quality awards. (In fact, say benchmarking experts, consider applying for an award even if you don't have a prayer; the process provides discipline, and it's a good way to get feedback).

PLAN TO SHARE. Getting your would-be partner to help is another matter. Direct rivals might be reluctant to share their methods, but others may embrace the idea if you don't come empty-handed, says Michael J. Spendolini, a benchmarking consultant in Laguna Beach, Calif. "Offer to give something in return," he says. For instance, if you're trying to improve your customer satisfaction process and you already have a great order system, plan to share it with your benchmarking partner.

If possible, conduct one or more on-site visits to observe and compare your partner's methods firsthand. You may

not be allowed to do hands-on work for liability reasons, but you still can learn enough to do a fair imitation back at your office.

Some owners may know which areas need improvement but are lost as to how to make the changes. That's where consultants can help. Fees can range from \$250 for an informal customer-satisfaction survey to \$75,000 for an in-depth, qualitative benchmarking study.

It's money well spent if you find the right person. Consider Master Mainte-

imates with a laptop computer. As generating more business, Bowers Eileen as an untapped resource. He suggested Master farm out the billing painting, which freed Eileen to bring in more revenue by doing estimates making cold calls. For good measure he suggested a Web site to increase their exposure, a tactic used by other contractors. But the most surprising suggestion was that the McGarry should stop bidding on every contract that came along and concentrate on the most profitable jobs. Today, the McGarrys aim to do work for large government agencies.

All told, McGarry's estimate that Bowers' advice will help Master more than double its revenue in the next year—which means his \$30,000 fee will pay for itself several times over.

As for Elfrid Foord, the financial adviser who wanted to survey her customers, she turned to Success Professionals Inc., a consulting firm in San Diego, Calif., that specializes in measuring best practices. "As a consulting firm, we give better answers than we were better able to analyze the data than if we did the survey ourselves," Foord says.

That \$5,000 survey was just the

beginning of her company's quest for best practices. Today, Foord says, her partners routinely benchmark by attending industry conferences, going to seminars, and networking among other professionals to find out better ways of doing business. "Benchmarking has become a way of life for our firm," she says. "It's a mind-set." It's also the habit of thinking that keeps you in front of the competition—a good place for a business to be.

By Toddi Gutner in New York

Benchmarking Resources

WEB SITES & SOFTWARE

▶ AMERICAN SOCIETY FOR QUALITY

(www.asq.org): Offers a best-practices data repository and a registry of consultants. Promotes networking with other benchmarkers.

▶ AMERICAN SOCIETY OF TRAINING & DEVELOPMENT BENCHMARKING FORUM

(www.astd.org): Provides a forum to benchmark training processes against other companies, statistics on training and development costs.

▶ AMERICAN PRODUCTIVITY & QUALITY CENTER INTERNATIONAL BENCHMARKING CLEARING HOUSE

(www.apqc.org): Provides articles, lists educational programs and studies, and offers research services available to help benchmarkers.

▶ DUN & BRADSTREET BUSINESSCOPE (software)

(software): Provides statistical analysis of similar companies, \$99.

▶ MANAGEMENT ROUNDTABLE

(www.trainingforum.com/MRT): Provides a forum for giving and receiving advice, network service, and articles.

▶ THE BENCHMARKING EXCHANGE

(www.benchnet.com): Offers surveys, market studies, and lists of best-practice companies.

▶ U.S. INTER-AGENCY BENCHMARKING & BEST PRACTICES COUNCIL

(www.va.gov/fedsbest/index.htm): Provides a calendar of benchmarking events; offers expansive list of related benchmarking Web sites and library resources.

▶ U.S. NAVY BEST MANUFACTURING PRACTICES

(www.bmpcoe.org): Offers case studies from corporations.

BOOKS

▶ BUSINESS PROCESS BENCHMARKING

by Robert C. Camp (ASQ Quality Press, Milwaukee, 1994, \$40)

▶ THE BENCHMARKING BOOK

by Michael J. Spendolini (AMACOM Press, American Management Assn., New York, 1992, \$19.95)

▶ BENCHMARKING FOR BEST PRACTICES: WINNING THROUGH INNOVATIVE ADAPTATION

by Christopher E. Bogan and Michael J. English (McGraw-Hill, 1994, \$29.95)

nance, a small paint-dealing contractor in Concord, Mass. "We knew we did good work, but we just weren't getting the jobs," says Bob McGarry, who started the five-person company with his wife, Eileen, in 1988. McGarry did a little benchmarking on his own with other contractors and learned that his bids took too long to work up, which in turn meant he had less time to solicit other business, and they needed to be more accurate. So he hired Fred Bowers to find the industry's best practices and set them up at Master.

After a month, Bowers was back with some answers. To speed up the bids, Bowers recommended doing on-site es-

For more on benchmarking resources, go to BW Plus! at www.businessweek.com or AOL keyword: BWEnterprise.

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MOVIE PALACE COUP

Harvard grads create a buzz building Mexican cinemas

Matthew Heyman had just one idea when he arrived at Harvard business school in 1991, fresh from a middle-management job in the cinema industry. He wanted to run a big theater chain. If he couldn't, he would start his own. It didn't matter where. "I asked everyone from every country," says Heyman.

Hearing of opportunities south of the border, he enlisted two Mexican classmates to help him transform his goal into a business plan. Together, they conceived the idea of building first-rate theaters in Mexico City, where the industry was in a shambles. The plan fulfilled a course requirement for their last semester, but to Heyman that was beside the point. "We're not doing this for a

grade," he told his class partners Adolfo Fastlicht and Miguel Angel Dávila. "We're doing this to do it."

Five years later, the trio has managed to turn its class project into a class act. Graduating from Harvard was the easy part. Since 1993, they have fought for financing, battled the local union, and weathered Mexico's worst recession in 60 years. Today, their company, Cadena Mexicana de Exhibición, or Cinemex, dominates the movie-theater scene in Mexico City, with 147 of the city's 416 screens and \$35 million in sales last year—about 40% of the city's ticket revenues. Its shareholders now include J.P. Morgan Capital Corp. and Hoyts Cinemas Groups of Sydney, Australia. "This was my shot at entrepreneurship," says

ENTREPRENEURS

THREE AMIGOS: Fastlicht, Heyman and Dávila "revitalized the industry."

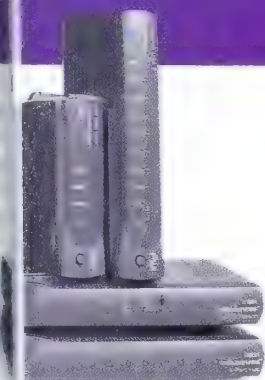
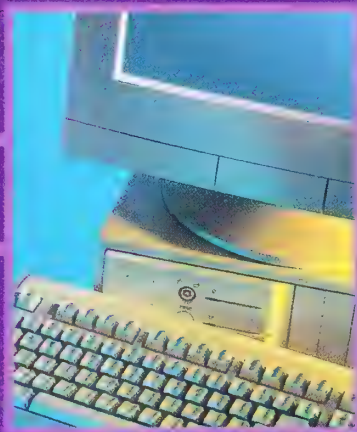
Heyman, the son of a TV salesman from Los Angeles.

Certainly, Harvard diplomas and local connections didn't hurt. But vision, persistence, and a feel for the local marketplace mattered more. "In a nutshell, they've revitalized the industry," says Luis Ruíz, sales manager for Videocine, a Mexican film distributor.

STALE POPCORN. The trio's timing was no accident. Their plans for Cinemex took shape as the government was ending decades-old price controls on tickets that had discouraged owners from upgrading their decrepit theaters. Sound quality was abysmal and the popcorn stale. Middle-class Mexican moviegoers had retreated to their videocassette recorders. Heyman bet that they'd go for top-notch sound, image, and service.

Even before the business plan was done, the three grad students began to bluff Cinemex into existence with more backing than their personal bank accounts. Fastlicht, now 31, used family connections in Mexico City's estate business to announce Cinemex was seeking space to lease—a bid to legitimize the venture to potential

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Companies

vestors. Meanwhile, Heyman, who at 29 had been making \$100,000 as Cineplex Odeon Corp.'s vice-president for business affairs in Toronto, unsuccessfully sought financial backing from his former employer.

Their money dwindled that semester as the trio racked up air miles back and forth to Mexico City. Heyman raided his savings account. Dávila, now 32, tapped the scholarship funds he had gotten for tuition. (As a result, he didn't get his diploma until he could pay Harvard back a year later.) By April, 1993, Heyman and his partners had finished the plan, but they needed \$6 million to bring it to life. A contact with A. Allen Friedberg, the retired CEO of what is now Sony/Loews Theaters, gave them entrée to chief executives of U.S. chains, but everyone turned them down. They finished up their MBAs; Heyman went home to his family in Los Angeles. Dávila and Fastlicht returned to Mexico City to raise capital. That summer, Dávila even turned down a job at Goldman, Sachs & Co. to pursue their goal.

WINNING COMBO. Cinemex' big break came in October, 1993, from an investment fund of J.P. Morgan & Co. Months earlier, at a Mexico City dinner party, a friend had told Fastlicht that an associate at Morgan's local office was interested in investing in movie theaters. Fastlicht gave him their plan, which eventually ended up with fund managers in New York. They liked the combination of Heyman's movie-theater background and the local expertise offered by Fastlicht and Dávila, who is well-connected in government circles. Says Tim Purcell, who runs J.P. Morgan Capital's Latin business from New York: "They were very impressive, and they had enthusiasm." Morgan Capital agreed to invest as much as \$8 million for 40% of Cinemex. With Morgan's backing, hesitant Mexican investors who had pledged only small amounts now signed on for more, while CMEX Investors, an affiliate of Chicago's JMB Realty, put up almost \$5 million. Altogether, Cinemex had \$21.5 million in startup funds.

Then, in December, 1994, before Cin-

emex could open its first theater, the government devalued the peso. The dollar value of what local investors had put up suddenly fell by half. But Heyman and his partners grimly pushed ahead. Soon, all of the international cinema chains—except Dallas-based Cinemark USA Inc.—had dropped their plans to enter Mexico; Cinemex had Mexico City almost to itself.

In August, 1995, the company opened its first multiplex in a new luxury shopping mall, investing \$3.5 million. But to revolutionize Mexican moviegoing meant

too? In May, 1996, Cinemex opened its doors in a poorer neighborhood. "If the deal wasn't going to work, our market was this big," says Heyman, his thumb and forefinger in a loose pinch. Tickets at that theater went for a dollar less than the others. Even then, with the average Mexican earning just over \$10 a day, Cinemex was expensive. Yet the strategy worked. Working-class families splurged on movie tickets and snacks as if they were "going to Disneyland," says Heyman.

HOMESICK. Cinemex' success has drawn new capital for expansion. In late 1996, Hoyts Cinemas, a publicly held company with theaters worldwide, bought a 35% stake in Cinemex for \$22 million.

Despite big-time backing, the three partners, who all go by the title of "director," remain firmly in charge. Heyman is the dealmaker and strategist. He attends film festivals, buys equipment, and negotiates with distributors. Dávila presides over operations, and Fastlicht directs the real estate department. Their deal with investors will give each of them a stake of just over 5%, probably by year's end.

What about competition?

Mexico rebounds, U.S. chains are piling in, while old local players regroup. "This is the city that has the closest risk of saturation," says Alejandro Ramírez, chief operating officer of Mexico's largest movie theater company, Organización Ramírez. In July, Ramírez plans to open his eighth Mexico City multiplex in a middle-class suburb. It will offer a café, child care, and a customer-service counter to call taxi and make dinner reservations.

The competition isn't scaring off Cinemex, which is confident it can maintain its lead. "We're going to own Mexico City," boasts Heyman. He figures the metropolis could eventually support 700 screens, with 400 belonging to Cinemex. At its current growth rate, Cinemex could reach that goal in a couple years. Then what? Heyman, admittedly homesick, says he would cash out the right price: "I would love to run a theater chain in the U.S.," he says. Enter Mexico City, that would be a cin-

By Elisabeth Malkin in Mexico City

CINEMEX' SCRIPT FOR GROWTH

MARKET An estimated 20 million people in Mexico City and its suburbs.

STRATEGY Build first-class multiplexes, and charge movie-mad Mexicans a premium for quality. Price tickets lower in working-class neighborhoods while maintaining luxury image.

MANAGEMENT Keep control in hands of three original partners while taking in outside investors.

GOALS Expand from 147 screens to 216 screens by end of 1998 and ultimately to 400; continue to expand in poorer neighborhoods.

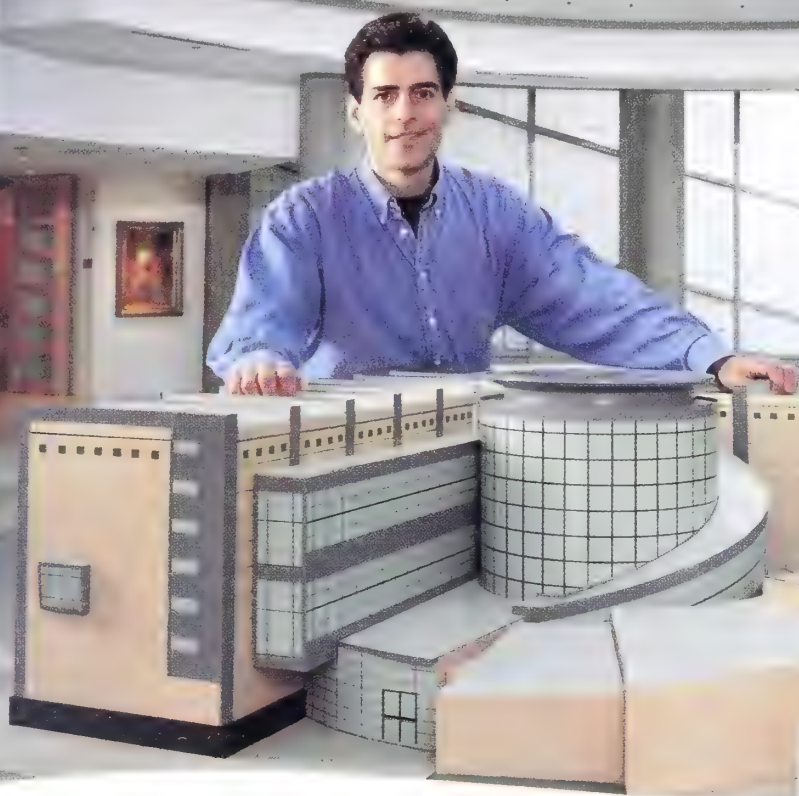
CHALLENGES Stave off new competition from U.S. chains such as Cinemark and General Cinema and giant Mexican chain Organización Ramírez.

first breaking the movie theater union, says Dávila. Rigid work rules had created massive inefficiencies: a popcorn seller, for instance, wasn't allowed to handle soft drinks. The union fought back, occupying the lobby with 150 protesters a few days before opening. Dávila hired security guards to keep the picketers out and then outflanked the union by opening on Wednesday rather than the expected Friday. The union moved the battle to the local labor board, but it ultimately sided with the company and recognized a more flexible union. Cinemex now has some 1,100 employees. About 65 work at headquarters; the rest, mostly students, run the theaters.

The buzz grew as Cinemex continued to open multiplexes. The theaters charged premium prices, about \$3.50, but even in the midst of recession, middle-class Mexicans seemed willing to pay for quality. Would the working class,

Heyman bet—correctly—that middle-class Mexicans would pay for top-notch sound and image

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SELLING THE SIZZLE OF...WATER?

Fountainhead hopes to package its way to profitability

You're a fledgling company in an exploding market. You think your product superior to rival brands, but most consumers can't tell the difference. You've no profits, little to spend on marketing, and about 500 competitors, from expansion-minded locals to global giants. You need big volume to break even. So, how do you boost distribution and get customers' attention?

For Fountainhead Water Co., the answer was packaging. After capping the first five-gallon jug

Fountainhead moved fast on its second choice, a tall, fluted bottle. Rolled out last spring, it won awards from industry groups and praise from consumers—and proved a hit with distributors and retailers. "You can have the best water; from a 3,000-year-old well, but that doesn't sell

PACKAGING

sustainable?" Rosenzweig, president of San Francisco-based Venture Strategist Group, was CEO at Republic of the Pacific in San Francisco, in 1992 when he introduced a canister imported from Japan. Within a year, competitors had similar canisters. Fountainhead patented its fluted design and extended it to most of the line. But not all design innovations are patentable. For example, neither the size nor the widened spout for easy pouring can be protected.

But even a temporary advantage can give a small company a leg up—and can be critical, particularly with a product as close to a pure commodity as water. Since 1993, Fountainhead has made yearly changes in packaging, picking

sales outlets each time. Eventually, distributors signed on when a six-pack of one-liter bottles was launched in 1994, pushing sales from less than \$1 million in 1993 to about \$4 million in 1995.

A squeezable sport bottle, introduced in 1995, brought in 35 more distributors. Likewise, the fluted bottle has lured major regional supermarket chains such as Kroger, Winn-Dixie, and Big Bear.

Killer packaging may cost more than advertising, but it's cheap. The fluted bottles

cost 2¢ to 5¢ more apiece than the mass-produced ones used by most water companies. Development costs add up, too: \$100,000 to make and re-jigger machinery for the sport bottle, and \$175,000 more for the flutes.

WARY PUBLIC. Those costs sting in an industry that competes on price—particularly as container costs account for 40% to 60% of what consumers pay. "Some of these costs we have to just absorb," McClanahan admits. But he thinks bigger sales will yield Fountainhead's first profit of \$500,000 to \$1 million this year.

In the long run, water quality will be key to building sales, analysts say. Having discovered that filtered tap water can be bottled and sold, U.S. consumers are becoming warier of contaminants. The Food & Drug Administration recently required labels that identify sources and treatment processes, and industry groups now give prizes for taste as well as packaging. Aware of the trend, Fountainhead is starting

to include taste tests in its marketing efforts. Will consumers notice the difference? Maybe. For now, Fountainhead is pleased they just notice the bottle.

By Edith Upchurch
in New York



from its Blue Ridge mountains aquifer in 1991, the Atlanta-based company expanded in the \$4 billion bottled water market with a flow of new designs. By 1996, sales hit \$5 million, yet profits remained elusive. President Kevin McClanahan sought a packaging breakthrough. The concept was a bottle with dual appeal: an unusual two-liter size—the recommended daily dose—and elegance for a dinner table. After choosing from 60 design proposals, Fountainhead spent \$25,000 on a prototype and tested it on shoppers in Nashville and Atlanta. "They hated it," says McClanahan. "They thought it looked like bleach, like kitty litter, anything you might not want your water associated with."

The bottle does," says Fred Sipper, president of New York beverage distributor Mootch & Muck Inc., which put Fountainhead in local stores.

"For an early-stage company, it's a very strong way to break through," says brand expert Bill Rosenzweig. "But is it



TRY, TRY AGAIN

The fluted bottle (left) replaced the 'bleach bottle' effort

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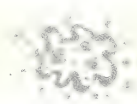
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COMPUTERS: TO LEASE OR NOT TO LEASE

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You can buy that hot new Pentium II desktop for \$3,000. Or you can lease it for only \$110 a month. Sounds like a great way to save money, right? So you do the math, multiplying \$110 by the 36 months of the lease, subtracting your tax break, comparing it with buying, and—whoops, leasing doesn't look like such a great deal after all. At best, you will have saved a few dollars or just barely broken even.

So why is the computer world going gaga over leasing, with rentals expected to double during the next five years? In a word, flexibility. Advocates say leasing lets you switch systems more often to

ure on three years before your desktop turns into a doorstop. At that pace, buying becomes a major burden for the typically cash-strapped small business. For instance, getting new computers for a five-person office could

tering his consulting office in Cornwall Bridge, Conn., where he creates special effects for corporate presentations. It's a field where technology rarely stands still for long. "My needs are always changing," says Selby. "I consider these things

MANAGEMENT

disposable after two years. So last year, he took out a 24-month lease on a state-

of-the-art laptop from Dell Computer Corp., and he fully expects to exchange it for a new one in 1999. Tech experts concede that you could come out a few bucks ahead if you buy a computer and resell it yourself. In reality, though, you'll probably waste valuable time on the sale and fail to get top dollar anyway.

SOUP TO NUTS. Which leases are right? They come in a dizzying array from independent leasing companies and retail stores. Some good deals are being offered direct from manufacturers such as Compaq Computer Inc. and Dell, with terms as short as 24 months. Typical plans run three years and give you the option to buy the machine when the lease expires at then-market prices for used equipment.

A more popular variation sets the option-to-buy price at 10% of the original retail value, making it easy to plan your budget. In practice, you might pay \$111 a month for a machine worth \$2,999, which pegs your purchase option at \$299. If, however, you're pretty certain you won't want the old clunker in 2000 when the lease expires, you

keep up with fast-moving technology, while leaving you with more cash to expand your business. It's a strategy with increasing appeal to small businesses, with about 12% already leasing one or more of their computers, says Raymond L. Boggs, an analyst at market-research firm IDC/Link. That's about the same rate as larger companies, says Joseph C. Pucciarelli, research director at Gartner Group, who expects one out of every four personal computers to be leased by 2002.

At best, Boggs says, you should fig-

mean coming up with \$15,000 every 36 months—a major blow to your bank balance or line of credit.

But if you lease, your cash hoard is left intact and available for growth opportunities. In effect, leasing serves as another source of financing.

When it comes time to get rid of the old computer, there's another advantage: You just ship it back to meet its maker. That would be just fine with Adrian Selby, who has four old computers clut-

THINGS CHANGE:

Your desktop may be a doorstop in three years

can skip the option to buy and save \$108 in payments over the duration of the contract.

Some vendors, such as IBM Credit, are offering soup-to-nuts packages previously available only to the large



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ENTERPRISE

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customers. The 36-month lease includes installation, six months of technical support, and the option to upgrade to new technology after two years, in return for a set fee. You can also add high-end services such as system monitoring and maintenance. The point: You can put a lid on all the other costs of owning a computer, which IDC estimates can exceed one-third of the machine's price.

Whichever lease you decide on, the total monthly payments can quickly top a computer's sticker price. But look at your final cost. Thanks to the Internal Revenue Service, you'll get a bigger tax break on leasing, because the fees can be deducted every year. By contrast, you would have to depreciate a computer purchase using a much less generous IRS formula. If you borrow to finance a purchase, that jacks up the final cost even more. The result? "Usually, there won't be a big difference at the end of the day between leasing and buying," says James M. Piazza, a tax partner at Arthur Andersen Enterprise Group.

LOWBALL? All the same, leasing has some real pitfalls. For instance, the seller could increase the sticker price or lowball the future value of the computer, which would raise your payments. And keep an eye on cash flow. Find out the annualized financing cost of the lease and compare it with the rate you could get on a loan. "If you can lease at a rate only slightly higher than what it would cost you to borrow and then to buy—say, 1%—then leasing is a better deal," Piazza says.

For instance, the \$111 lease cited above costs the equivalent of 23% annually—not bad if your alternative is the 22% interest charged by CompuSA for its in-house credit card. But it's pretty steep compared with 15% on the best small-business credit cards. And if your business has cash earning 2% in some bank account that isn't going to be used

for some other purpose, then leasing doesn't make a great deal of sense. "It isn't the answer all the time," says Ralph Mango, a vice-president at IDC Financial Services.

Thinking about breaking your lease early? Don't. Most contracts force you to pay the remaining installments or exact a large penalty (although some companies may cut you a deal if you're looking to upgrade). Also, make sure you stop thinking about how you're going to replace the machine six months before the lease expires, says Gartner Group's

Pucciarelli. Otherwise, the deadline will arrive, your whole life will shift on that computer, and you'll have no choice but to sign a lease extension—boosting your total cost far beyond what it would have cost to buy. And under any circumstances, expect to pay the freight when it's time to ship the computer back. At today's rates, that's typically about \$80.

What's the basic rationale for leasing? If you don't have to spend on the cutting edge of technology, it's better to buy. Some companies use computers mostly for word processing and don't get material from outside companies created with newer software. In that case, a computer will probably still be useful long after its third birthday.

Brian D. Brumit, a tech specialist at Coopers & Lybrand LLP, points out that you can also use a combination of leasing and buying to minimize costs. This means leasing the hottest machines for the top technical people who constantly need upgrades and buying less advanced machines for office workers doing low-tech jobs like simple typing who "can make do with second best," says Brumit. Assuming, of course, that the superheated competition generated by technology doesn't raise the bar for "second-best."

By Beth McGoldrick in Boston

THE LOGIC OF LEASING

Reasons to lease a computer instead of buying:

TO SAVE CASH

There's no big sum to lay out. Your bank account and borrowing power remain untapped, so you'll still be able to jump on new opportunities.

TO SAVE ON TAXES

The cost of a lease can be deducted, which reduces taxable income.

TO SAVE TIME

A leased computer can simply be shipped back. By contrast, finding a buyer for an old computer takes time from your regular work, and you're not likely to get top dollar.

TO SAVE YOUR NECK

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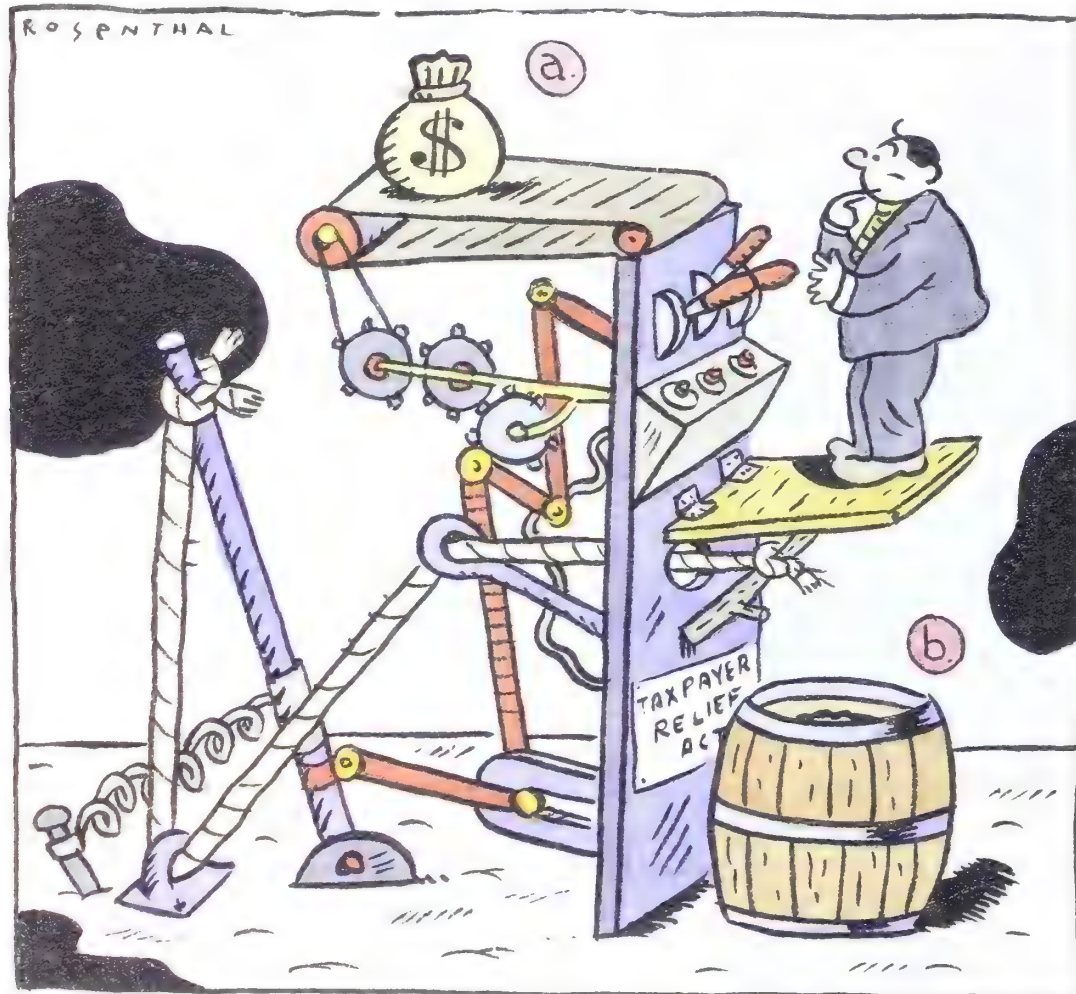
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PANNING FOR GOLD IN THE NEW TAX CODE

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smaller companies don't do much in reality, Diesslin adds.

Some gems have emerged, however, especially from innovations that were specifically designed with small businesses in mind. One example is the Roth IRA, which unlike the conventional IRA doesn't impose a tax on withdrawals. Because business owners have more control over their income than ordinary wage earners do, they have more of an opportunity to shelter income under the income limits and thus reap the benefits.

Even minor changes such as the \$500 increase in the equipment-expense deduction are welcome at a time when computers seem to become obsolete the day after they're delivered. Truly creative owners can maximize the benefit by taking out a loan to finance the purchase as late as

After reading the 1997 Taxpayer Relief Act, Susan Ginsberg and Gene Myers decided that 1998 was the year for their small Chicago CPA firm to splurge on two new, automatic feed-and-sort photocopy machines. "It's a luxury we had always done without, but we decided to treat ourselves," Gins-

The purchase lets Ginsberg Myers & Associates take advantage of an \$18,500 tax deduction for office equipment bought in 1998, up from \$18,000 last year. More important, it helps them hold their individual incomes under \$100,000

in 1998. In turn, this makes them eligible to convert their tax-deferred IRAs into Roth IRAs—which is worth thousands of dollars in tax savings. Says Ginsberg: "Spending on office equipment is a way to have our cake and eat it, too."

That's the kind of ingenuity it takes to squeeze a break from the tax rules that take effect this year. "The law tinkers with everything, but doesn't make major changes," says David Diesslin, a Fort Worth financial planner who specializes in helping small businesses. Some of the breaks targeted for

Dec. 31. Even though you haven't laid out a dime yet, the law lets you take the full \$18,500 deduction in 1998—a classic case of deduct now, pay later.

Want another double play? Relate carefully between the lines on health insurance. This year, the premiums are 45% deductible for the self-employed. That's up from 40% in 1997—a deduction that inches up to 100% by 2007.

If you don't want to wait, say the experts, hire your spouse. Sole proprietors can't fully deduct their own policies, but they can deduct the full cost of

TAXES

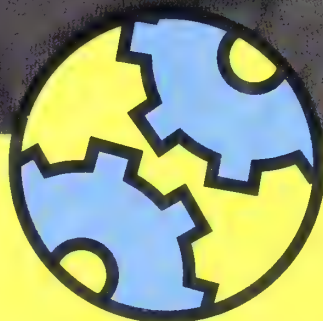
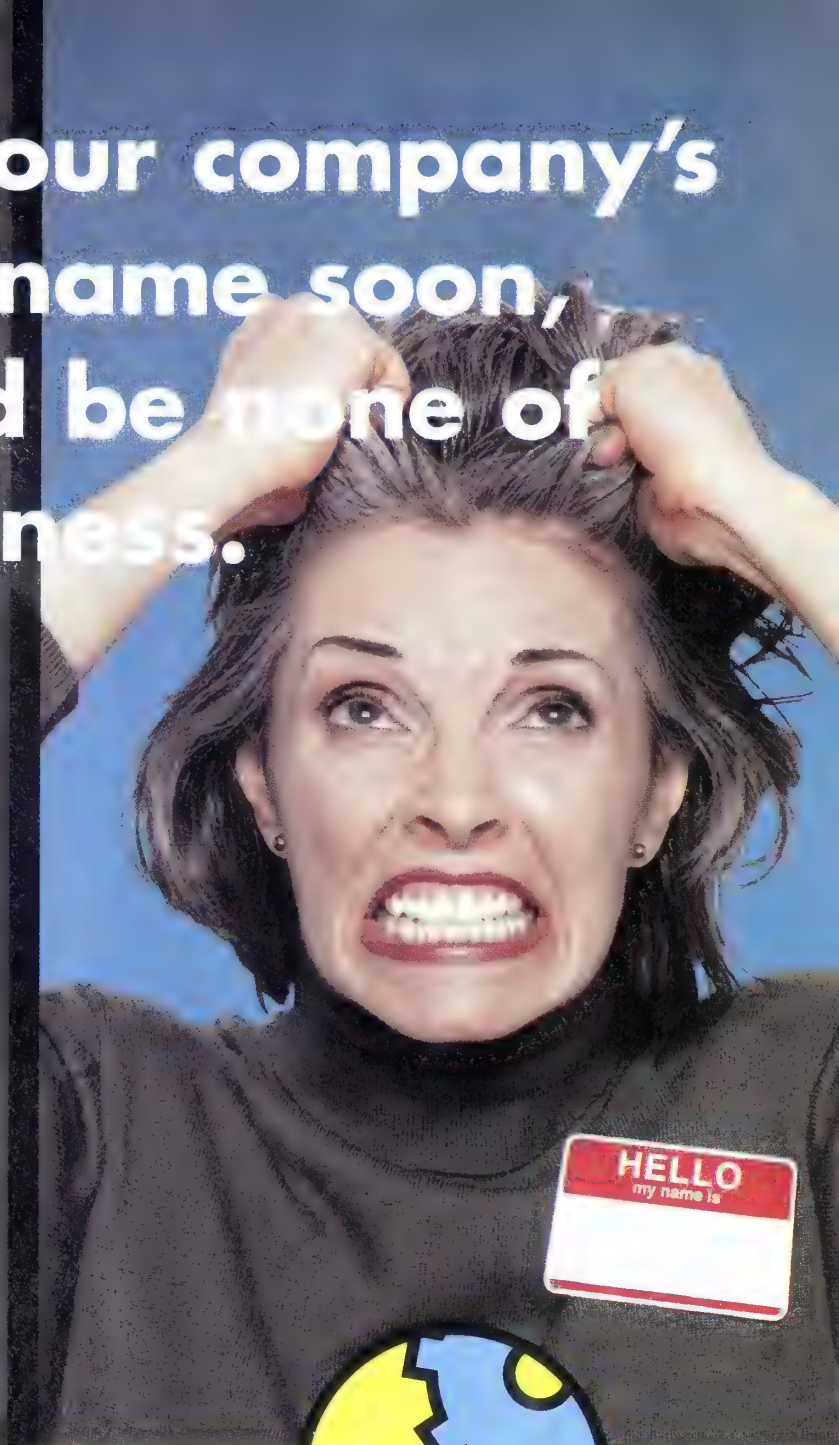
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There's also a break on capital gains for serial business owners—those who sell off one venture and roll the money into another. Instead of shelling out the standard taxes on your profit, you can defer them from the sale of small-business stock if you use the money within 60 days to buy stock in another small business. There are some conditions, though, says James Caskey, an Indianapolis tax accountant: You must have acquired the stock at original issue, held it for at least five years, and sold after Aug. 5, 1997.

DON'T BOTHER. Most of the other ballyhooed small-business breaks are likely to disappoint, despite the fanfare when they passed. How about the new \$1.3 million estate tax exemption for small family-owned businesses and farms? It's a nonstarter, says John Dadakis, an estate-law expert at Rogers & Wells in New York, because the burdensome rules outweigh any benefit. Besides, Dadakis adds, the exemption is worth less each year; it's offset by the standard estate tax exemption, now at \$625,000, which is increasing in stages to \$1 million by 2007.

Similarly, the new law exempts small companies from the Alternative Minimum Tax if their average annual gross receipts were \$5 million or less in 1995, 1996, and 1997. But practitioners say

such businesses seldom paid the AMT anyway. "I've never seen it happen," says Ed Slott, a tax accountant in Rockville Centre, N.Y. A new charitable deduction for corporations that donate computers to schools won't be of much practical value either, says Kyra Hol-lowell Morris, a tax planner in Mt. Pleasant, S.C., because you have to have some tax basis left in the equipment—not very likely, she says, since small businesses tend to write the equipment off quickly.

The experts are more interested in some of the more general changes that could benefit small-business owners disproportionately. For instance, the dramatic cut in capital-gains tax rates for individuals—they'll drop to as low as 8% by 2005—is an excellent reason to give company stock to your children and grandchildren now instead of risking federal inheritance taxes that run as high as 55%, plus any state levies. And the Roth IRA is practically made to order for small-business owners, who have many ways to lower and defer income.

Just don't get too creative. Deferring income and accelerating expenses to

squeeze under the \$100,000 limit this year will raise your 1999 income—and 25% of the amount you withdrew from tax-deferred IRAs to finance the Roth IRA will be added to your 1999 income. "Your 1999 tax bracket could go from 28% to 36% as a result," Caskey says, so you will wind up paying more. Worse still, if the IRS later disallows some of your deductions as too aggressive, it might retroactively push your 1998 income over \$100,000, warns Slott—and that would disqualify you for a Roth IRA.

Speaking of legal problems, don't rush to open a Roth if you have any reason to worry about lawsuits. Most state laws protect investors from creditors, but federal statutes refer specifically to tax-deferred IRAs, not Roth IRAs. Advise

Seymour Goldberg, a Garden City (N.Y.) tax lawyer and pension specialist: Wait until your state updates its laws. Otherwise, the Taxpayer Relief Act may turn into another headache, and you can't deduct the aspirin won't be deductible.

By Lynn Brenner in New York

Where It Hurts

What's the most burdensome levy for small business? Payroll and personal income taxes, says a recent poll.

BIGGEST TAX BURDEN

PAYROLL TAX	41%
PERSONAL INCOME	37
CORPORATE INCOME	11
CAPITAL GAINS	6
ESTATE	3
OTHER	2

DATA: ARTHUR ANDERSEN ENTERPRISE GROUP

Brenner is the author of Smart Questions to Ask Your Financial Adviser (Bloomberg Press, 1997).

CAREFUL—THAT KEOGH MAY BE HOT

It's so clever it sounds illegal: Convert your Keogh plan to a tax-deferred IRA, which the old law allows, and then use the new law to convert that into a Roth IRA. Pay the fees, and *voilà*—your major retirement asset is now tax-free.

Well, it is legal. The problem is that your Keogh might not be—a fact that thousands of account holders will have to confront even if they don't try to convert to an IRA.

The problem is most likely to affect the thousands of Keogh plans sold by brokerages, mutual funds, and banks during the past decade. The most common flaw: Plan documents were not amended to conform with routine changes in the law since 1986, because the institutions that sold the plans failed either to stay on top of

the requirements or to notify customers. Nor did they have much incentive to do so: As custodians rather than fiduciaries, the institutions aren't liable for the violations, says Seymour Goldberg, a Garden City (N.Y.) tax lawyer who specializes in pensions. "I'm seeing this with two-thirds to three-quarters of my new clients—one plan after another that's no good," Goldberg says.

It's unclear just how many Keoghs are at risk; at last count, there were 900,000 accounts with 1.4 million participants, according to Spectrem Group in San Francisco. But illegal plans are so prevalent that last month the IRS said it will allow owners to come clean in exchange for a limited range of fines. The maximum penalty for a business with fewer than 11 em-

ployees: \$4,000. The ceiling hits \$8,000 for up to 50 workers and \$12,000 for employers of up to 100.

By IRS standards, it's a good deal. If your company is audited, the maximum penalty is loss of the tax benefits derived in the prior three years. If you roll an illegal Keogh into an IRA and get caught, the entire amount is immediately taxable because it counts as a withdrawal, notes Goldberg. "There's also a 6% fine for each year you maintain the illegal IRA, with no statute of limitations," he says.

If you bought an off-the-shelf plan and didn't sign any plan documents between 1992 and 1994, says Goldberg, you'd better raise the issue with your advisers. The IRS may not be so forgiving when you're ready to retire.

By Lynn Brenner

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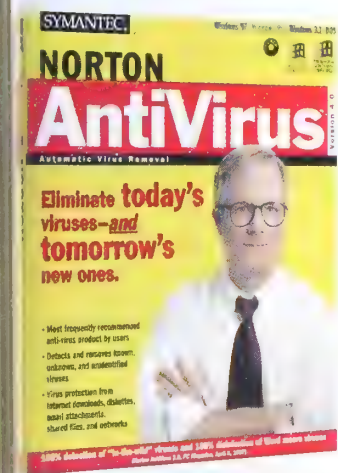
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DEALING WITH CONFLICTS AT HOME

A talk with relationship counselor Azriela Jaffe

It's a dilemma that's faced by many entrepreneurs: How do you keep a marriage strong while meeting the round-the-clock demands of a small business?

Azriela Jaffe, 38, has been on both sides of the quandary. First, she endured the launch of her husband's accounting firm. Then, two years later in 1995, she abandoned a 15-year human resources career in banking and social services to start her own business, *Anchored Dreams*, from her Lancaster (Pa.) home. There she publishes an international online newsletter for entrepreneurial couples on business and relationship issues (www.isquare.com/az4.htm) and coaches couples in phone and online sessions. She is the author of *Honey, I Want to Start My Own Business* (HarperBusiness, \$23).

Enterprise's Dennis Berman recently spoke with Jaffe—shortly before the birth of her third child in three years—about the impact a new venture can have on spouse and family.

Q: What drove you to write your book?

A: It's essentially the book that I wish we had read before my husband quit his job. At the time, my husband and I were both masters-level professionals in corporate jobs—your basic dual-career beast. My husband, at my encouragement, decided to leave his job to start his own business out of our house. And if the business had launched the way we had hoped, and everything had been rosy, I suppose I would be on an entirely different path. But the fact is, the transition for my husband from being employed in a corporate job to being self-employed was harder than we ever expected—on him, on us as a couple, and on our family.

Q: When did you realize that things weren't going as planned—and what occurred when you reached that point?

A: One of the first things that happened is that our financial projections for my husband's business were way

off, and we were unprepared for how we were going to handle that. I don't care how many women proclaim they're now feminists. My experience is that most women have difficulty being the primary provider for their family. And it was very hard on my husband's ego to suddenly be cast in the role of not being the primary breadwinner.

WORK & FAMILY

Q: There seems to be a fine line between supporting a spouse while also being realistic about the spouse's entrepreneurial dreams. How do you do it?

A: There is a conversation that couples absolutely need to have from the very beginning of the process, where they're clear with each other about the kind of sacrifices, financially and emotionally, they're willing to make.

The spouse who is becoming unsupportive, belligerent, angry, resistant, or downright crabby about what's happening in the business is very often not getting his or her concerns addressed. And those concerns may be something as simple as, "I don't feel like we have enough insurance," or "I'm worried that we're going to lose the house." And if

FIRSTHAND: Jaffe, mother of two, endured the start of her husband's business before launching her own—advising entrepreneurial couples

that person doesn't feel like they have the ability to have a dialogue with their spouse, then they start getting even more resistant and put the brakes on the whole process.

Q: What's the worst that can happen when these communication breakdowns strike?

A: One woman who contacted me had lost her home, even her pets, because she and her husband had to move from

a house to a rental property. They had very coveted trust fund that she had relied on for years but was now dwindling down to what she felt to be almost nothing. Her husband was running his business into the ground. What made the situation so painful was that the marriage was disintegrating because he didn't even want to come home any more. When he did, he had nothing but a very angry, frightened spouse who kept rubbing his face in his failures.





his gets down to a couple of basics. One is that this couple had not established a way to set boundaries with each other. She had no way to say, "this is too much," or "this has got to stop." They were just ignoring each other. When I lost touch with her, the business was still not profitable, and he was ready to give up on it.

You mention in your book that entrepreneurs starting a business can be a spouse experiencing some of the stress an affair might provoke. At times it can very much feel like there is, out of a sudden, a third person in the marriage. If you just take the sex out of everything else is there. You've got something or someone totally occupying your fantasies and your dreams, your thinking and your time.

Q Before a spouse jumps into entre-

preneurship, would you recommend the couple draw up a written agreement outlining boundaries and expectations?

A: If you are willing to, writing it down always helps solidify the commitment. But I hesitate to say every couple should do anything.

Q: What about a "contract" with the kids?

A: That brings up one of the tragedies of entrepreneurial life: One reason for starting a business might be to spend more time with your family, then the business takes over your life. One of the best ways to make sure that you don't lose touch with your family is to identify the things that hold it together, be it having family dinners at night or going to church on Sunday.

Q: What particular qualities have you found that help couples handle the hav-

oc of entrepreneurial life?

A: A lot of what makes a strong entrepreneurial couple is what makes a strong marriage in the first place. What may not be so obvious, that I certainly have discovered, is that you've got to have a sense of humor about all this. If you take entrepreneurship too seriously in your marriage, you're going to end up going crazy. You should appreciate and enjoy the business, but you shouldn't be so attached that if it should change you're going to fall apart.

Q: What types of businesses take the greatest toll on family life?

A: Retail is the worst when it comes to locking you into certain hours. I remember very vividly a couple I interviewed that was running a Mailbox Etc. business and had put it up for sale. They didn't think through what it would actually feel like, six days a week, to be sitting in a Mailbox Etc. office. They felt really trapped in the business.

Then the other issue, when you're dealing with a manufacturing business, is the amount of investment and capital that's required. And very often, the financial risks and losses are much more dramatic when you're dealing

with high-tech or manufacturing businesses than when you are with smaller home-based services.

Q: How can starting a business strengthen a marriage?

A: The point is that you've found your right livelihood, whether it's working together in a business or whether one or both of you are self-employed. As much as we can talk about the downside of self-employment, we can also acknowledge that a spouse trapped in an unhappy corporate job is not good for a marriage, either. So, in the best-case scenario, both members of the couple are thriving in their work lives and then they are gaining a certain amount of freedom, independence, and control over their lives, and that dramatically enhances a marriage.

Join Jaffe for a live chat on Apr. 19 at 9 p.m. EST. Go to AOL at keyword: BWTalk.

WHEN A PHONE HEADSET IS THE RIGHT CALL

Good ones can prevent workplace injuries and make workers more productive

Talking on the phone can be a pain in the neck—literally. Just ask Jean Dunn, the branch manager for Interim Personnel Power, a temp agency in Lackland, Mo. She spent so much time with the phone awkwardly balanced between her head and shoulder that by the end of the day, her muscles were in constant pain. "I would go home and rub on the Flex-All and just eat a lot of ibuprofen," says Dunn, who was visiting a physical therapist up to four times a month.

Then, two years ago, she bought a telephone headset. The pain eventually faded away, and the physical-therapy visits ended, too.

Such workplace injuries aren't uncommon in modern offices. Susan J. Isenrath, a consultant with Duluth (Minn.)-based Isenrath Work Systems who specializes in work-related injuries, says casual phone users can be victims, too, if they have sloppy posture that puts an undue strain on muscles. Headsets help avoid that problem and can make workers more productive by leaving their hands free.

But not every model will do the trick. You should expect to pay about \$150 to \$200 for a commercial-grade unit that includes a headset and accompanying amplifier. "Some who are slightly savvy balk at the price because they think they can go to RadioShack and buy one for \$50," says Steve Seltzer, an efficiency expert in Harvard, Mass. "If you do that, you'll

OFFICE TECH

get a headset that doesn't fit very well and people who won't use it."

Good fit isn't the only consideration. Headsets come—or don't come—with a host of options, including one or two earpieces, noise filters, quick-disconnect cables, and mute buttons. Some are clearly sturdier than others, a major consideration if you spend most of your day on the phone. And sound quality can vary from superb to downright tinny.

You'll also need to consider the design and how you'll feel about wearing it.

Dunn already had received a headset from the corporate office, but she had shunned it because the headband style messed up her hair—a concern when meeting clients. The headset that eventually satisfied her could be worn simply draping it over her ear.

Which headset you pick depends on what kind of office you're running. If it's a noisy place with a lot of people in the same room, a headset with two earpieces will make it easier to hear and a noise-canceling device in the microphone will ensure that the person on the other end can't hear the cacophony, either. If the headset will be used in a high-visibility location, such as a reception or customer-service area, image can be as important as sound quality. And if you spend a lot

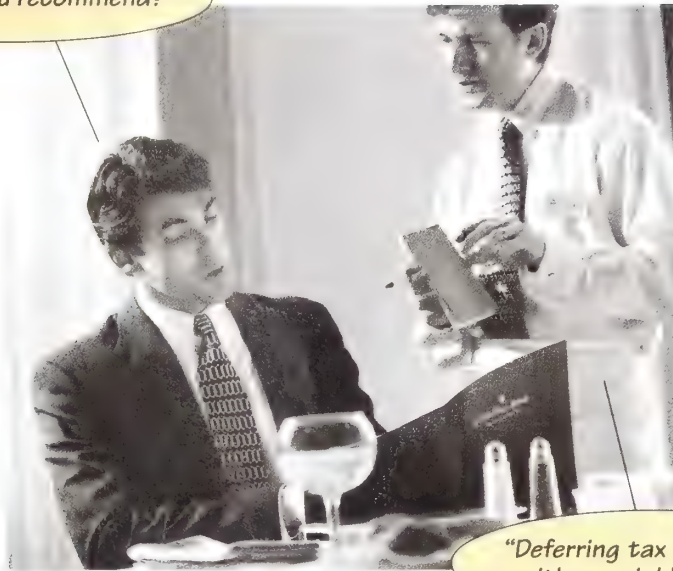
time away from your desk, a cordless model may be the answer.

NO-BRAINER? With these possibilities in mind, we looked at a dozen commercial models, all from leading headset manufacturers and available through distributors and the mail. We also tested a couple of consumer models sold at retail stores.

If price were the only consideration, models such as the RadioShack HS-1000, currently available for as little as \$49, would be the no-brainer buy. But it was noticeably less comfortable than more expensive headsets, and our testers said the sound was more muffled. It also comes without conveniences such as a quick-disconnect, which allows you to untether yourself from the phone when



"What do you recommend?"



"Deferring tax obligations with a variable annuity."

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Buyers Guide

out having to remove the headset.

Given the bargain price, it might be good enough for infrequent users. If you're on the phone all day, though, check out the GN Netcom/Unex Optima OPT-1N and ACS Wireless Inc.'s Applause Monaural (which, despite the company's name, is not cordless). Some callers said they heard our testers more clearly on these headsets than on a regular phone handset, perhaps because of the noise-canceling feature found in both models. The Applause suppressed background sounds so well when the headset user wasn't speaking that the caller on the other end could barely hear a radio blasting in the background.

COMFORT ZONE. Both the Optima and Applause feature headband-style designs, which we found to be more effective in helping us hear clearly and in limiting distractions from background sounds. But you may not want to base your decision on audibility alone. The headbands on the ACS Wireless Stratus Ultra and GN Netcom/Unex's Profile 405-FLEX proved much less comfortable, and while the headband on Hello Direct's UltraLight Pro fit well enough, its stiff plastic boom was hard to adjust.

In a high-visibility location where image counts, a headband won't do. Instead, you'll want a headset that looks

sleek, sounds excellent, and is easy to remove. With these criteria, the edge goes to the Plantronics TriStar, an over-the-ear model that combines clear sound with unobtrusive design. Most of the other models were the antithesis of sleek, especially ones that featured spongy mi-

crophone booms that extended from up to 150 feet away, along with decent sound quality. It's not compatible with digital phone lines, but a compact called KONEXX (800 275-6354) offers a \$225 adapter that bridges the gap.

Even then, cordless headsets may not be appropriate for everyone. G

Use Your Head

Which headset is best? The answer depends on how you plan to use it. List price includes amplifier and noise canceler; all come with mute buttons and volume controls.

MANUFACTURER	MODEL	LIST PRICE/TYPE STYLE	PHONE #	WHY BUY
RADIOSHACK	HS-149	\$30/Cord Headband	800-843-7422	Low price
PLANTRONICS	TriStar	\$128/Cord Over ear	800-544-4660	Good looks
ACS WIRELESS	Applause Monaural	\$206/Cord Headband	800-995-5500	Heavy use
GN NETCOM/ UNEX	Optima OPT-1N	\$206/Cord Headband	800-345-8639	Heavy use
PLANTRONICS	CT-901-HS	\$225/Wireless Both	800-544-4660	Mobility

DATA: BEACON RESEARCH GROUP INC.

crophones that look like big black acorns floating in front of your face.

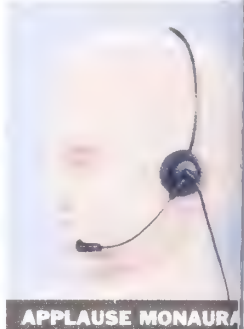
Cordless models go beyond being merely hands-free. Untethered to the phone, you can carry on a conversation as you walk over to a file cabinet or down the hall to the water cooler.

In this category, another Plantronics model stood out, the CT-901-HS, because it has controls that can dial and cut off

No matter which model you choose, one thing does make sense: putting down the receiver—for good.

By Mie-Yun Lee, editorial director, BuyersZone (www.buyerszone.com), Boston

For more information on headsets, go to www.businessweek.com or AOL at keyword BWEnterprise.



APPLAUSE MONAURAL

gory T. Moffatt, a criminal lawyer at Boston-based law firm Foglio, Hoag, & Eliot, says ruled out cordless models because wireless could be picked up by eavesdroppers. "It just makes sense not to broadcast these conversations," he says.

WIRING YOUR CAR PHONE FOR SAFETY

Saving your neck takes on a whole new meaning when it comes to car phones. Critics call them a major safety hazard—and they won't get any argument from Brian Senory, who sells telephone accessories for Tampa-based SenCommunications. He was taking down directions on his cellular phone in February, 1997, when he rolled right through a red light, hit another car, and caused \$3,000 in damage. The irony: His own product line includes wireless headsets for use on cellular phones. "I never felt I had a need for one," says

Senory, who now counts himself as a customer.

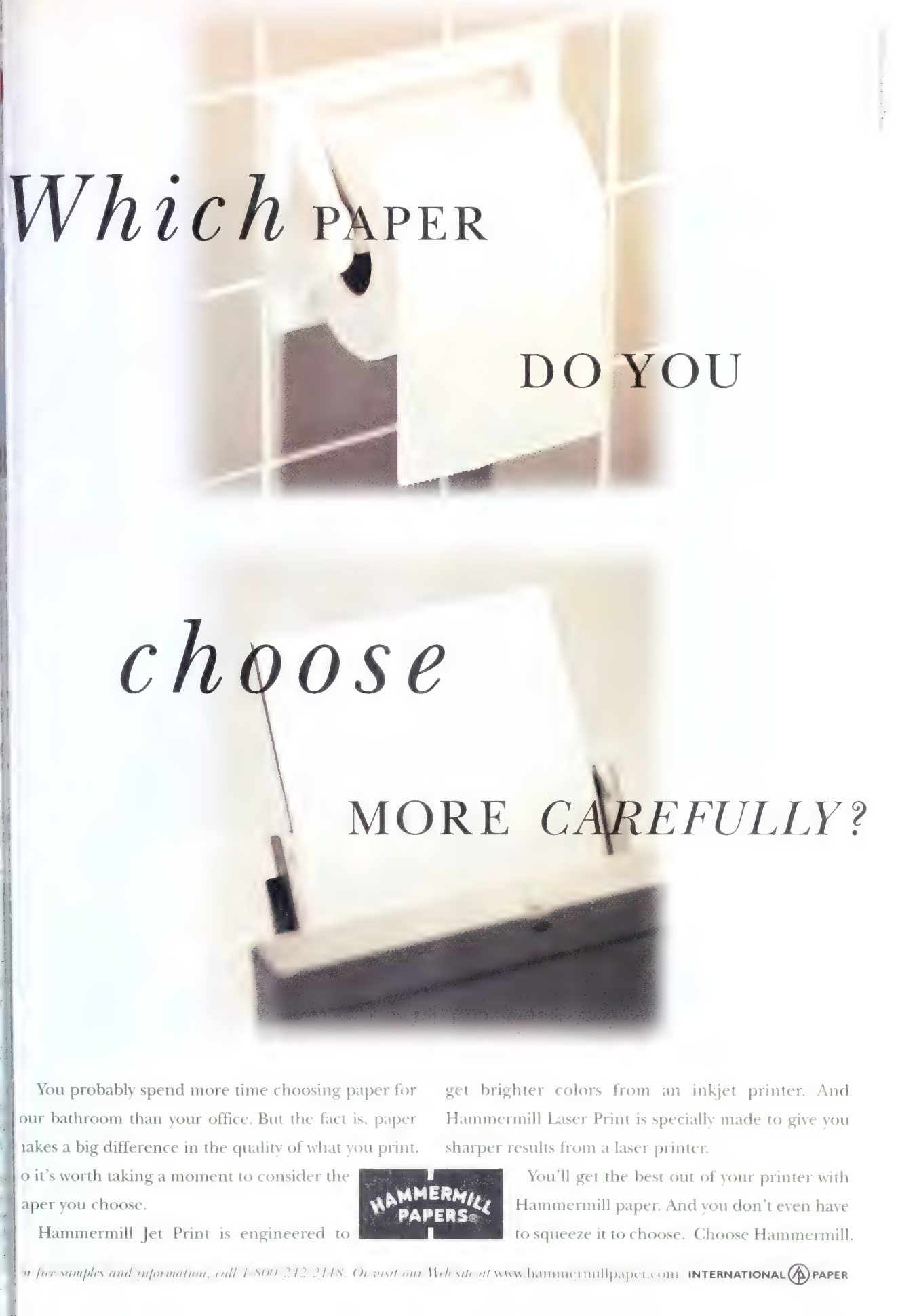
The good news is that cellular headsets are inexpensive, retailing for as little as \$20. Much like office models, car-phone headsets leave both your hands free, and their noise cancelers can eliminate most of the road sound that afflicts models with microphones mounted in the cab. Check your cell phone for a headset jack; if it doesn't have one, some phones can be retrofitted with a special adapter for about \$40.

Of the ones we tested, the \$60 Plantronics CHS142-N had the best

outgoing sound quality. With a traditional design that plants the microphone close to your mouth and a noise canceler, background traffic sounds were effectively muffled. You can wear it over the ear or as a headband.

You'll hear a little better with the \$40 Jabra EarSet. This clever design hangs the microphone and speaker from a plastic earpiece that rests comfortably inside your ear. It comes with three different sized ear gels to ensure a comfortable fit, and the result is somewhat better reception for the driver.

Mie-Yun Lee



Which PAPER

DO YOU

choose

MORE CAREFULLY?

You probably spend more time choosing paper for your bathroom than your office. But the fact is, paper makes a big difference in the quality of what you print. So it's worth taking a moment to consider the paper you choose.

Hammermill Jet Print is engineered to



get brighter colors from an inkjet printer. And Hammermill Laser Print is specially made to give you sharper results from a laser printer.

You'll get the best out of your printer with Hammermill paper. And you don't even have to squeeze it to choose. Choose Hammermill.

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Chances are you didn't go into business to fulfill a lifelong of busywork.

From: Microsoft Office 97 Small Business Edition
Sent: Monday, 9:00 a.m.
To: Everyone who has to do everything
Subject: How to do it.

helps you save time on the work that needs to get done, so you can spend more time on the work you actually like to do. So, pound away on letters and documents knowing Office 97 Small Business Edition is following along, correcting your spelling, watching your grammar, and generally helping out when you need it. Pull up your budget and accounting numbers and analyze them in ways that make it easier for you to make informed decisions. Use the Microsoft Outlook™ integrated e-mail program to keep in touch with customers and vendors and stay on top of your schedule. And because Office Small Business Edition includes Microsoft Publisher 98, you can create your own professional-looking newsletters, brochures, business cards—even Web sites. In other words, Office 97 Small Business Edition is a suite of smart, easy productivity tools, linked together to help you do your best work and circumvent the busywork. To learn more about it, and to find out about the free* product enhancements and assistance you can get through Microsoft Office Update, visit

DOWN TIME

Heard Any Good Books Lately?

TO HONE YOUR LEADERSHIP SKILLS OR SALES TACTICS, JUST HIT THE 'PLAY' BUTTON



Speaking from his car phone, Jim C. Suttles says, "My whole day is a commute." As a national marketing rep with Partners Title Co., a 45-employee mortgage title company in Houston, he spends much of his time visiting clients. But the hours en route aren't wasted. Suttles hones his professional skills listening to taped versions of best-selling business books. "It's a great way to stay up on things," he says.

Suttles is not the only one keeping up by keeping his ears open. Audiobooks are a \$2 billion business, up from \$250 million a decade ago. And while books on tape used to be mostly fiction, today there's a substantial selection of business titles. "It's an incredible growth area," says Anne Gaudinier, executive editor of the HarperAudio division of HarperCollins Publishers Inc. Of the 63,000 books available, the Audio Publishers Assn. estimates that 25% to 30% are business-related. Some are instructional, teaching sales techniques or leadership skills. Others entertain and inspire, such as *Ben & Jerry's Double Dip*. Biographies of entrepreneurs such as Sam Walton are also popular.

PEP TALKS. Tapes are the only way R. Jeff Sayers, the time-pressed owner of a fledgling pizzeria chain in Austin, Tex., can finish a book. He recently enjoyed *Pour Your Heart Into It* by Starbucks Corp. CEO Howard Schultz. Sayers identified with the author's early struggles and was reassured by his ability to overcome. "It's good to hear a success story and know it's possible to make it," says Sayers, who bought copies of the tape for his managers. J. Michael Savage, an audiobook fan and partner at the law firm Maynard, Cooper & Gale, even keeps a mini-library of tapes in his office, from which clients and employees of the Birmingham (Ala.) firm are welcome to

sor of education at Vanderbilt University. At Heller Audiobooks in Manhattan, lot of the customers are Wall Street types who listen to motivational audiobooks to "get pumped up" before the morning bell, says owner Robert L. Heller.

There is one potential drawback, though. Most audiobooks are heavily edited to keep down prices and listening times, so taped versions may not be as complete as printed books. An unabridged reading of Jan B. Stewart's *Den of Thieves* for example, costs \$104 and is 19.5 hours long. The abridged version is a more reasonable 3 hours and \$16.00—about average in price and length. At the low end, a one-hour abridged tape of *The Way of Real Wealth* by Mark Waldman costs just \$5.50. For the truly time-pressed, \$135 a year buys taped synopses of two titles per month from Audio Tech Business Book Summaries Inc. in Chicago (800-308-TALK).

CHEESES AND BOOKS. Audiobooks are widely available and a growing number of retailers also rent them, for about \$4 per week. Clubs such as Columbia House (800-965-9665) and Audio Book Club Inc. give discounts of 15% to 70% to members who commit to a set number of titles. Road warriors can even stop at outlets of Cracker Barrel Old Country Store Inc., which have carried audiobooks—popular with truckers—since 1993. Cracker Barrel books can be returned for a refund, minus \$3 for each week that the customer has kept the tape at any of the chain's 330 outlets in 34 states.

No matter where you get your hands on them, business audiobooks can be a great investment. Suttles calls the tapes "career development made easy." That's enough to make any entrepreneur all ears.

By Kate Murray
in Houston

ROLL THE TAPE

Here's a sampling of places to look for audio business books.

AUDIO BOOK CLUB
www.audiobookclub.com
888 567-AUDIO

HELLER AUDIOBOOKS
www.helleraudiobooks.com
800 218-8181

EARFUL OF BOOKS
www.earful.com
800 5-EARFUL

TERRY'S WORLD AUDIOBOOKS
www.idsonline.com/terraflora/audio

(DATA BUSINESS WEEK)

Besides saving time, audiobooks can offer another advantage over paper ones. Many business book authors are also professional speakers and record their own work. Hearing *The Pursuit of Wow!* from Tom Peters

may be more inspirational than reading it. "Certain speech patterns can excite people and make them more likely to attend to the material than they would otherwise," explains Robert D. Sherwood, associate profes-



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What's it going to take for your office of five to serve your clients like an office of fifty?

Maybe you need a Lucent small business phone system. We specifically design our phone systems to meet the needs of businesses like yours. With features such as built-in caller ID and voicemail you'll be more accessible, more efficient and therefore better able to take care of your customers' needs. Plus, our systems are designed to grow easily as your company grows, and are backed by a wide choice of service programs. We're with you for the long haul. So even with a handful of employees, to your customers you'll be big-time all the time. To set up an appointment, just give us a call today at 800 325-7466 ext. 332 or contact your local Lucent Authorized Dealer. **We make the things that make communications work.™**

Every customer likes to be treated as if they're the best customer you have. That's why you need a Lucent small business phone system. We specifically design our phone systems to meet the needs of businesses like yours. With features such as built-in caller ID and voicemail you'll be more accessible, more efficient and therefore better able to take care of your customers' needs. Plus, our systems are designed to grow easily as your company grows, and are backed by a wide choice of service programs. We're with you for the long haul. So even with a handful of employees, to your customers you'll be big-time all the time. To set up an appointment, just give us a call today at 800 325-7466 ext. 332 or contact your local Lucent Authorized Dealer.

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Bell Labs Innovations

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Basking Ridge, NJ 07920
1-800-325-7466 ext. 332



Pocket Flashlight

The handy new ZipLight pocket flashlight teams a replaceable battery pack with any classic Zippo case. Customer response has been overwhelming for ZipLight, voted most popular new Zippo product of the year!

Zippo Chic

Fashionable and functional, the new ZipLight features the same sound, feel, and personality as the familiar Zippo lighter.



Brush Chrome finish with two-color surface imprint

Business Gift

Thousands of companies have made Zippo products their choice of gifts for decades. Our imprinting techniques are among the most advanced in the business, and our quality is second to none.

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Now, for a limited time, when you order custom imprinted ZipLight pocket flashlights, they'll each come in an attractive combination gift box with an extra battery pack ... FREE!



zippo

To place an order, or for more information, call 1-800-254-4481 (press 1 at prompt) or fax 800-362-3598. But call today, this offer ends June 30, 1998!

Catalog minimums apply • Made in USA

ZipLight

pocket flashlight • personal treasure

THE NEW RATINGS GAME

For all the techno-savvy out there, measuring traffic on the Web remains a very inexact science

When executives of SportsLine USA Inc. sat down in March to review their marketing strategy with America Online Inc., they didn't anticipate spending an hour poring over conflicting data on how many people visit their Web site. After an exasperated session, both sides decided to chalk off that part of the review, ditch the numbers from different rating companies, and come back later. "We aren't getting anywhere—we weren't even looking at the same measurements," says Kenneth Dotson, SportsLine's vice-president for marketing. Such knock-down fights over measuring Internet traffic are all too common. While the Web has been trumpeted as a virtual marketplace where advertisers could target precise demographic groups and gather reams of data on buying habits, the reality is altogether different. Today's technology just isn't up to snuff, and advertisers still can't aim their Web ads any more accurately than they can in print magazine ads. Worse, even basic measurement techniques for sizing up the most popular Web sites are so varied that a list of the top 25 sites is intensely disputed.

ILISHLY DIFFICULT. The problem this time is more than just data frustration. Reliable measurement methods are essential for the Net to become the advertising bonanza Web-site operators are banking on. By 2002, online ad revenues are expected to hit \$9 billion—a fold jump from the \$1 billion spent in 1997, says Jupiter Communications. Advertisers say they have been holding back, in part, because of differing tallies. "It affects ad spending when you see these discrepancies in numbers," says Jean Lehoullier, managing director at Cy Interactive Worldwide, an ad

agency with 71 clients, including Dell Computer, and Procter & Gamble.

Web sites measure their own popularity, largely by the number of "hits," or the times a page or parts of a page are called up. Sites then try to convert that into "unique visitors," so that one person calling up several pages is not counted more than once. That's an inexact science, and advertisers want precise—and impartial—data.

That's devilishly difficult. Figuring out how to zero in on specific groups of buyers is improving, though the Holy Grail of laser targeting by age, income, and past buying habits is generally still out of reach (page 78).

Even the easier target of measuring the number of people visiting a Web site is a tough slog. For the past couple of years, Media Metrix Inc., founded by market research firm NPD Group Inc.,

The next 18 months should shake out which services—and techniques—win out



was the only game in town for tracking the popularity of sites. Now, the company is being challenged by a band of rating-service wannabes. Last fall, upstart RelevantKnowledge Inc. began nipping at the leader's heels. On Mar. 30, NetRatings Inc., a startup backed by Hitachi Ltd., launched a rival service. And this summer, PC Data Inc., which tracks hardware and software sales, and Nielsen Media Research, of TV research fame, are joining the fray.

The snag: Each uses different methods for monitoring usage, which produces conflicting results. Consider February's tallies: The lists of the top 25 Web sites put together by RelevantKnowledge and Media Metrix shared only 19 names. And while both ranked the search engine Yahoo! in the top three, they varied on the other two top slots. "I think no data is better than wrong data, especially when the industry is saying we can be an effective medium," says Marshall Cohen, president of Marshall Cohen Associates, an entertainment and Internet consultant.

The differences start with the survey groups. Each service has a group of people, or "panel," who agree to install software on their PCs to monitor their movement online. Media Metrix recruits its panel by buying population

lists and conducting random mailings and phone calls. Some 45,000 people have agreed to take part in its surveys, but only 30,000 actually do. Of those, 9,400 were Web users in February. Media Metrix executives say that by enlisting PC users who are not all Netizens yet, they can track people as they start to come online.

NO-NOS. RelevantKnowledge, in contrast, relies on random phone calls to recruit people who already use the Web. While 11,000 have agreed to be part of RelevantKnowledge's survey group, only 4,000 usually participate.

The size of the sample can be crucial. While the Nielsen TV panel of 5,000 peo-

vice-president of consumer and strategic research at the Weather Channel. NetRatings defends its practice of recruiting right off the Web, saying a savvy panel gives more useful results.

The varied sample groups are only one of the ingredients that contribute to conflicting data. Another issue is that none of the services adequately factors in people who use the Net at work. Tracking firms miss up to one-third of Web usage if they focus only on the home, says IntelliQuest Inc., a technology market-research firm. "The tough thing is that so much of what we do is business-to-business advertising, and none of the services do a good job giv-

tions aimed at making the software less intrusive.

International Web users also get short shrift. RelevantKnowledge began working with a Swedish partner in March, and the other services have plans in the next year to attack the problem. "That's important to us," says Sean Pfister, director of research and analysis at CN Inc., whose technology news and search sites get between 8% and 15% of the traffic from international users.

The new ratings services may be muddying the waters for now, but the added competition is expected to lead to more reliable measurements. Media Metrix already has been forced to slice data

RATINGS HERE, THERE, AND EVERYWHERE

MEDIA METRIX

TOP-RATED PROPERTIES:*

1. 
2. 
3. 

The pioneer of Web ratings relies on a survey group of 30,000 people who have software installed on their PCs to track usage. Ratings are based on reach—the percentage of visitors at a Web site each month vs. the total number of Web users.

NETRATINGS

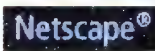
TOP-RATED PROPERTIES:†

1. 
2. 
3. 

Uses the Web to recruit a sample group that's expected to rise within a year to 25,000 people, from 2,000 at launch. Presents data in a variety of ways, such as listing top sites by most page views (or times a page is loaded into a browser) per person.

RELEVANTKNOWLEDGE

TOP-RATED PROPERTIES:**

1. 
2. 
3. 

Signs up survey group, now made up of 11,000 Net users, via phone. Plans this year to expand to 20,000 people, in part by going international. Its data show the number of first-time users who visit a site each month.

NIELSEN MEDIA RESEARCH

Plans to begin offering data this summer. Survey group now numbers 3,500 and is expected to reach 10,000 by yearend. Group selection made through random-digit phone calls. Hasn't decided yet how it will slice data. Plans to track Net usage on non-PC devices, like TV set-top boxes connected to the Internet.

* Group of sites rated from home in February

† Group of sites rated week of March 15

** Group of sites rated in February

ple is plenty for the 52 cable and network channels it monitors, small sample sizes for monitoring the Web make it difficult to track usage beyond the top 200 to 300 sites. Ad agencies and Website operators say that, ideally, they would like to see panel sizes of at least 10,000 people.

The latest company to join the measurement game, NetRatings, already is drawing criticism. Its sample group of 2,000 pales next to that of Media Metrix, although NetRatings expects within a year to have 25,000 participants. And some potential clients fret that its group is recruited off the Web—which can tilt results toward heavy users, rather than a cross-section. Self-selection for survey groups also is considered a no-no, because it means the process of selection isn't random. "Those of us who are conservative researchers wouldn't call something that's self-selected a sample," says Jim Alexander,

ing information on that," complains Alan May, media director at Anderson & Lembke Inc., the agency that handles Microsoft Corp.'s Web ads. In March, RelevantKnowledge included about 700 Web users at work, while Media Metrix included 850. All three plan to expand work coverage, but admit difficulties.

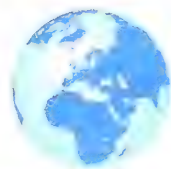
The problem lies in convincing companies that it's O.K. for employees to install tracking software on their computers. This software is more sophisticated than cookies, the tiny software programs commonly used by individual sites to monitor usage. The fear is that the software can potentially trace identities, as well as confidential data, such as memos or sales information. "If people are concerned about cookies, imagine how they would feel about this technology," says Manish Bhatia, vice-president for interactive services at Nielsen, which won't audit work usage initially, although it's developing technical solu-

ways comparable to rivals. By June, the company plans to offer home and work data combined. That's something RelevantKnowledge already provides. NetRatings and RelevantKnowledge also are beefing up their ability to track America Online Inc.'s subscribers, who account for 40% of all Web usage from home. Today Media Metrix tracks all of AOL's subscribers, while its rivals have limited access. The reason: AOL executives say they are hesitant to give carte blanche to new tracking companies without details on their methodologies.

EARLY BETS. Other forces also are working to standardize ratings. This month the Advertising Research Foundation formed a committee of companies to use the ratings services. The objective is to look into how the services operate. "At the minimum, the idea is to understand what the companies are doing. It's unclear now," says James Spaulding, president of the foundation, a nonprofit



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too much
to fly you
only to Paris.



Despite what our name may imply, Air France flies to 102 cities in Europe and 189 worldwide. Our international hub at Charles de Gaulle is easy to navigate so you can quickly transfer to frequent connecting flights. And if you have any questions while you're there, just ask any of our employees. They may work for a French airline, but they'll answer you in plain English.

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AIR FRANCE

WINNING THE HEARTS OF THE WORLD





"TO THE OUTSIDE WORLD THIS IS A PIZZA COMPANY. TO ME, IT'S AN ENTERPRISE."

NET PROFILES

MATTHEW MAGUIRE

038

SOFTWARE
NOVELL DIRECTORY SERVICES
MANAGEWISE
HARDWARE

DIRECTOR,
INFORMATION TECHNOLOGY

DOMINO'S PIZZA®



WORK OF MULTIPLE PLATFORMS, PROTOCOLS AND USERS. EITHER WAY WE DELIVER."

Matt Maguire knows all about delivery. His company delivered over 226 million pizzas last year. And with 4,500 stores across the country, Matt's network had to deliver the same superior performance and reliability that made Domino's® the world's leader in pizza delivery.

To do that, Matt chose Novell® networking solutions. NetWare® software as the core server operating system. NDS™ technology to manage his other operating systems, including SCO® UNIX® and Windows NT®. ManageWise® to support all 1,200 remote devices in his network from a single location. And GroupWise® messaging services to leverage the ubiquity of the Internet to give employees worldwide access to their email.

All in a seamlessly integrated system that could adapt to the changing needs of the business and scale up as it grew.

The result? On-site technician calls were reduced to twice a year, administration tasks were performed in minutes instead of hours, money was saved, productivity was increased, employees stayed in touch, and Matt looked like a genius.

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SOLUTIONS

group that encourages marketing and ad research. Media Metrix also has met with the Media Rating Council, which accredits ratings services that disclose their procedures and abide by them.

So, which method will win out? In the next 12 to 18 months, a front-runner is bound to emerge. For one, the sheer cost of using the services, which can range from \$40,000 to hundreds of thou-

sands of dollars annually, will force Web-site operators to be selective. "Our tactic this year is to buy all the data that looks valuable, get really knowledgeable about it, and then next year drop what we don't think is worth paying for," says Karen Edwards, Yahoo! Inc.'s vice-president for brand marketing.

Early bets are on Media Metrix, because it leads the pack, with 150 clients,

and has the biggest survey group. Although Nielsen is late to the party, its brand name and resources have caught advertisers' attention. "Media Metrix is the front-runner, but nobody has got it right yet," says analyst Charron of Forrester Research Inc. That means there will be more data angst before the Web measures up.

By Heather Green in New York

TRACKING WHO SURFS WHERE

The Internet hasn't delivered on one-to-one marketing—yet. But a raft of services are becoming ever more sophisticated in helping advertisers target ads and track their effectiveness. "We're constantly learning more about which eyeballs are going where," says Norman Lehoullier, managing director at ad agency Grey Interactive Worldwide.

To do this, advertisers rely on a variety of services. They mix and match the ratings information from companies such as Media Metrix Inc. with data from other companies such as Excite Inc.'s MatchLogic, or AdKnowledge.

These services let advertisers and Web-site operators serve up ads to specific audiences and then assess the response.

FOLLOW THE LINKS. How is the information used? Ask Fragrance Counter, a Brentwood (N.Y.)-based cosmetics retailer, which during the past two quarters used ratings info from Media Metrix and Relevant-Knowledge to select sites that were popular with women. Fragrance Counter then added its proprietary technology to figure out how successful its ads were.

The result: Ads linked to keyword searches, such as "perfume" or "Estée Lauder," as well as to the shopping areas on search engines, were among the most effective. Ads in the CNET Inc. shopping area, for example, had a "click rate," or percentage

of people who clicked on the ad, of 4%—compared with less than 1% in the Yahoo! local-content area. And the percentage of people who bought a product was 3% in the Yahoo! shopping guide, vs. less than 1% in the local-content area. "From what we've learned, we'll pay significant cash for the placement we want," says Eli Katz, vice-president for marketing at Fragrance Counter.

Still, the information advertisers can get is limited. Most of the ad-tracking services are confined to collecting such data as which browser a cybersnaut uses and what country he or she lives in. That's pretty slim, although it does the trick for technology news service CNET Inc., which uses such data to target Windows-based software ads at Windows 95 users. Another way to aim

ads is through a method called "context"—monitoring the overall content a cybersnaut is viewing and serving up ads accordingly. If someone is searching on the keyword "car," for example, a General Motors Corp. ad might pop up.

Getting precise demographic information is the most difficult. That's because it's still hard to get wary consumers to provide personal data such as age, income, and sex. One way Excite is attacking that problem is by running online sweepstakes—a gimmick that puts cybersnauts in the running for prizes like vacations to Florida in exchange for personal information. "This helps advertisers introduce

more knowledge into their decisions," says Craig Donato, Excite's vice-president for database marketing.

Other services are attacking the problem more broadly by trying to track usage across many sites. CMG Information Services Inc.'s Engage plans later this month to introduce an ambitious service called Engage.Knowledge, which will start off with 10 million profiles of Web users. These profiles will be collected from a host of sites, including search engine Lycos Inc., that monitor usage on their Web sites. The data collected by Engage.Knowledge can be sliced into 800 categories, including sports and hobbies, for advertisers and Web-site operators. It's far from advertising nirvana, but it's one step closer.

By Heather Green in New York



DONATO: *Prying info out of consumers with online sweepstakes*

Congratulations to the
of the Thirteenth Annual
Business Week Awards
for Excellence in Corporate Advertising



The readers of Business Week have recognized twelve distinguished advertisers for creating the best-remembered corporate campaigns of 1997.

The winners were determined based on 1997 advertising readership scores compiled for Business Week by Roper Starch, an independent research firm and the acknowledged readership measurement standard for the print industry.

Business Week is proud to recognize these companies for excellence in corporate advertising and award them with a symbol of excellence, the Steuben crystal eagle.

Representative ads of the winning campaigns are shown on the following pages.

Amoco Chemicals

ENRIQUE J. SOSA, EXECUTIVE VICE PRESIDENT, CHEMICALS SECTOR
BENDER, BROWNING, DOLBY & SANDERSON ADVERTISING, CHICAGO, IL



**PROPELLING KAYAKERS
INTO THE FUTURE
REQUIRED A STROKE
OF GENIUS AND
AMOCO AMODEL**

Amoco and Aquabound, a Canadian sports equipment manufacturer, are teaming up to meet the demands of a rapidly growing sport by making a new kayak paddle that's cost effective to mass produce. Aquabound uses Amoco's new Amodel PPA* in a gas assist injection molding process. Buoyed by Amodel's high flexure and tensile strength, excellent creep resistance, low moisture absorption and stiffness, Aquabound dramatically reduced the wall thickness of the hollow paddle. The result is a lightweight blade that can withstand a real beating from rocks and gravel, and the stresses of rushing water currents and marine growth.

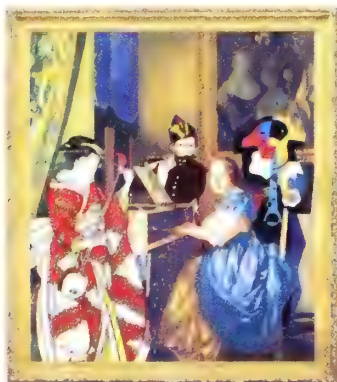
This broad range of characteristics is also propelling Amodel into a wide variety of other applications.

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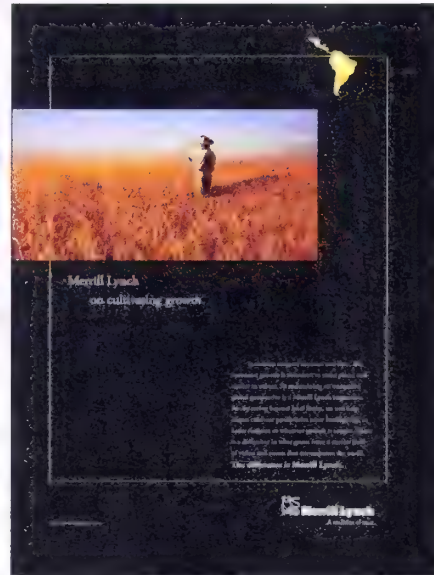
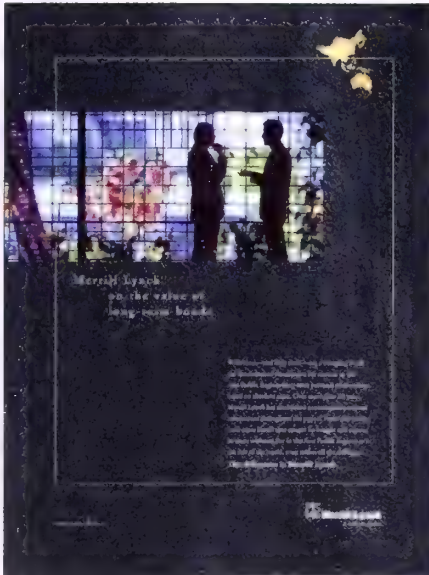
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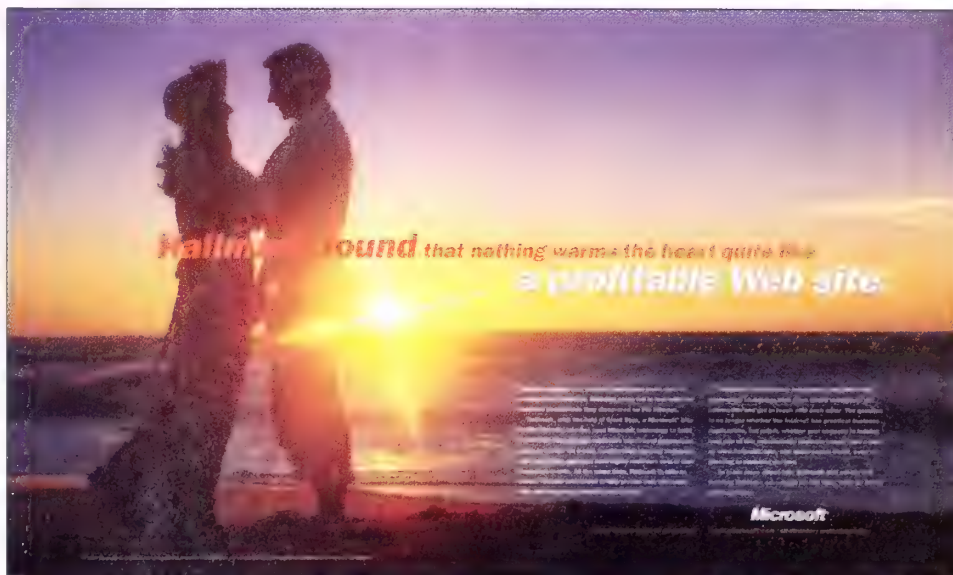
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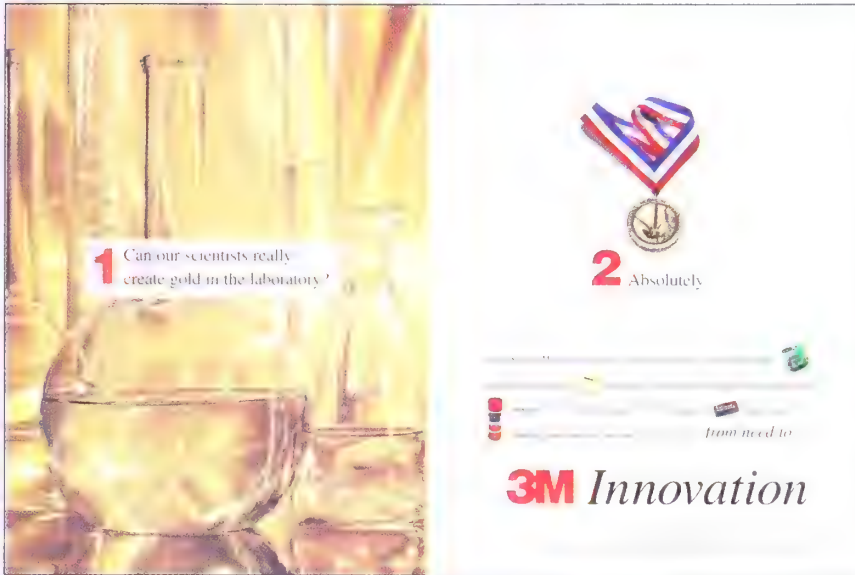
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PRIME TIME OR PRIMESTAR?

ould soar if Justice finally clears its News Corp. merger

For four years, the powerful cable companies that own PrimeStar have the broadcast satellite service as a kind of safety blanket. In the eyes of rural viewers, it's a way to sign them when they couldn't get cable. And for urban viewers, most of whom already subscribed, the service was to nab the few satellite customers who would otherwise bolt to competing direct broadcast-satellite (DBS) services. In both cases, cable couldn't lose.

Now, as its DBS rivals EchoStar Inc. and EchoStar Communications Corp. pick off growing numbers of cable customers, PrimeStar wants to stay for keeps. It is urging the government to approve a \$1.1 billion merger agreed to

May with Rupert Murdoch's News Corp., which, along with MCI Communications Corp., controls key satellite slots and uplink facilities. The gambit is crucial for PrimeStar. A decision by the Justice Dept. to block the alliance would leave PrimeStar the high-powered satellite slots it needs to match services offered by rivals. Yet the government is under pressure to be tough, since approving the deal, even with conditions, would give cable-TV interests a foothold in high-powered DBS, the only real competition for the big cable franchises across the U.S.

Under review since July, the case is coming to a head, say sources close to the talks. In a matter of weeks, the companies are expected to meet with U.S. Attorney General for Antitrust William F. Klein. Lawyers close to the case expect him to either nix the deal outright



BEAMING UP: With a merger, CEO O'Brien sees "a national business"

or demand strict safeguards, such as a consent decree requiring PrimeStar's cable-TV owners to sell programming to rival DBS operators on equal terms. The Federal Communications Commission must also approve the deal.

CABLE CONNECTION. For PrimeStar, the merger with Murdoch is vital just to stay afloat. Although it has signed up 2.1 million subscribers since 1994, second only to DirecTV's 3.5 million, PrimeStar uses a medium-powered satellite and offers only 160 channels, about two-thirds that of its rivals. It can't provide Internet services and requires dishes twice the size of competitors'—averaging 36

inches in diameter, a turn-off for suburbanites and city dwellers.

But if the deal is okayed, PrimeStar would gain control of 28 satellite slots MCI won at auction in 1996 for \$682.5 million. (MCI and News Corp. teamed up then to compete in satellite TV; MCI technically holds the license.) That would give it 29% of the high-powered transponders that can blanket signals across the continental U.S. PrimeStar President and CEO Dan O'Brien says the company plans to compete aggressively on price and hopes to double subscribers, from 2.4 million projected for the end of 1998 to 5 million by 2002. "PrimeStar knows the industry really well and has relationships in place, so the new slots would make them remarkably competitive," says DBS analyst Jimmy Schaeffler of market researchers The Carmel Group in Carmel, Calif.

Still, there's no dodging the cable connection. With the public mad about cable rate hikes, which last year rose at four times the rate of inflation, it's no wonder regulators are looking askance at the proposed merger. The concern is that allocating scarce DBS spectrum to cable interests may not be in consumers' interest. "Congress has an explicit policy to promote competition to cable.

The last thing we'd want is to allow the very companies that are monopolists to dominate this alternative transmission medium," says Gene Kimmelman, co-director of the Consumers Union in Washington. Indeed, PrimeStar's investors would seem to have an inherent conflict of interest with DBS. After all, they are the five biggest cable players: TCI Communi-

SKY WARS

Regulators will soon rule whether PrimeStar can use News Corp.'s satellites, extending cable's reach in high-powered DBS

COMPANY	SUBSCRIBERS MILLIONS	TRANSPONDERS
DIRECTV/USSB	3.5	35
PRIMESTAR	2.1	28*
ECHOSTAR	1.2	22

*Assuming News Corp. merger goes through
DATA: DBS INVESTOR

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Media

cations, Time Warner, Comcast, Media One, and Cox Communications. Together they serve 67% of all cable homes and produce much of the content as owners of such units as Home Box Office, the Discovery Channel, and CNN. Its in-house programming muscle would be even stronger in the event of a green light since News Corp.'s channels, including Fox's news, sports, and movie services, would be included. "PrimeStar's owners have such a complicated array of interests that it is impossible to engage in anticompetitive activities," says PrimeStar's attorney, Philip Verveer.

CARTEL But to critics, it all adds up to a strong incentive for PrimeStar's cable owners to deny programming to rivals and offer shows only at unfair prices. PrimeStar hasn't helped overcome any mistrust by marketing mainly to rural consumers while shunning existing cable subscribers. In 1997, only 15% of its new subscribers were won over from cable compared with 55% for DirectTV, according to The Carmel Group. Says Charles W. Ergen, CEO of rival EchoStar: "We don't believe the five biggest cable companies... should be able to form a cartel. It won't do anything but raise the price of programming to customers."

PrimeStar execs are hoping their plan to restructure and go public will go a long way toward assuaging critics. If the merger goes forward, 20% of all shares would be spun off to the public, creating an independent bloc of shareholders that could sue if management failed to pursue new customers vigorously. News Corp. would have a 30% nonvoting stake, and senior managers would get options tied to subscriber growth. Rather than sitting on the scarce spectrum space or favoring rural subscribers, "the goal is to have a national business and national economies of scale," O'Brien says. Even so, the government's leash will be short if it gives the nod. It will almost certainly require equal access to programming produced by PrimeStar's owners. And it may also monitor subscriber growth in cable strongholds and demand outside directorates on the board.

Such terms wouldn't keep a merger of PrimeStar from extending cable's reach deep into DBS, making life tougher for DirectTV and EchoStar. That would satisfy PrimeStar's owners, who ultimately care more about getting paid for programming than how it is delivered. But it would be a bittersweet win. Even as they reached more subscribers via satellite, many of those new viewers would be pulling the plug on cable.

*By Steven V. Brull in Los Angeles
with Catherine Yang in Washington*

{Spectrum Policy}

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THE EURO

In one fell swoop, it will create the world's second-largest economic zone. The potential benefits are limitless—and so are the risks

It was a dream of European visionaries. From the devastation of war, a modern Europe would be rebuilt with diverse cultures but seamlessly linked economies. Great corporations would arise in a common market, and workers would prosper as never before. Someday, when a fully integrated Europe was in place, they would cap the achievement by giving everyone a crisp single new currency to replace those faded marks, francs, lire, and pesetas.

It never happened. Europe's economies remained as Dutch, German, French, and Italian as ever, and its nations prospered better than anyone dreamed by rebuilding their national markets. The U.S. wanted a strong Europe to fight communism during the cold war. The Europeans put their military into NATO, but governments clung doggedly to their own national power. An exasperated former Secretary of State, Henry A. Kissinger, famously asked: "When I want to talk to Europe, who do I call?"

Now, all that is about to change. In a bold step toward eventual political union, Europe is launching a monetary revolution. On May 2, 11 countries—Germany, France, Spain, Italy, Ireland, the Netherlands, Austria, Belgium, Finland, Portugal, and Luxembourg—will set the terms under which they will trade in their national money for an untested currency, the euro. They are sacrificing a fundamental element of sovereignty—the right to issue their own money. Instead, a European central bank will run the European monetary union. Members will also surrender two of their most powerful economic safeguards—the right to devalue out of trouble or run budget deficits to counter mass

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THE NEW FINANCIAL MARKET

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THE NEW ECONOMY

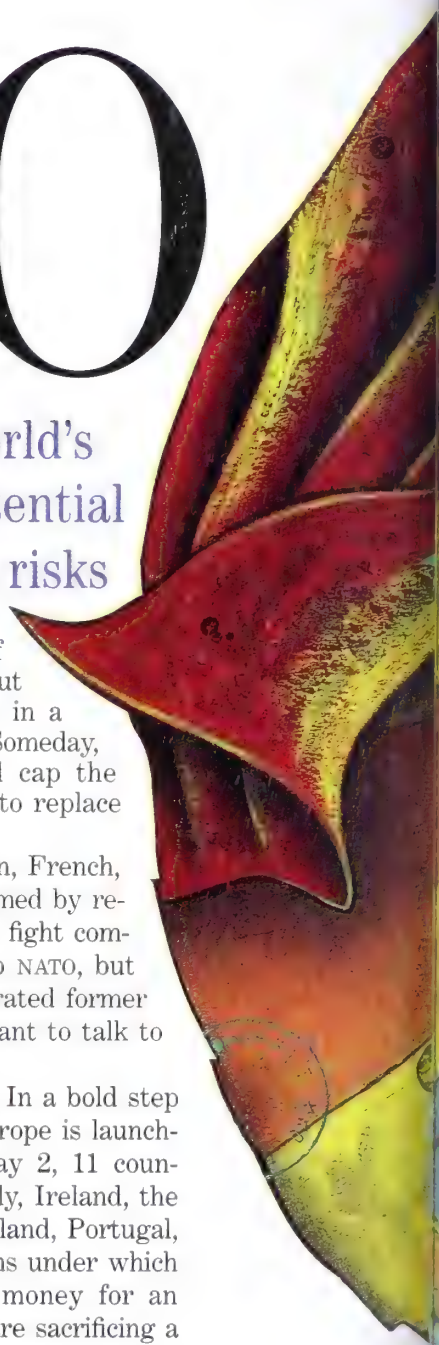
Industrial Evolution *Page 100*

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COMMENTARY

Can the Cultures Mix? *Page 108*







unemployment. In essence, they have handcuffed their government spending, tax policy, and bond and stock markets to a European future. The only way out is to quit, and no nation shows signs of doing that. The economic tremors could shake Europe to its foundations. The reform is likely to unleash an unstoppable market process that will sweep away structures Old Europe held so dear—national corporations and banks, rigid work rules, generous pension payments. In their place could emerge a competitive \$6.4 trillion economy, second-largest in the world. “Monetary union is going to be the catalyst for Europe’s revival—economically, politically, and in self-confidence,” says Leonhard Fischer, a board member of Dresdner Bank.

JOB THREAT. But the risks are so great and the consequences of failure so far-reaching that many outsiders remain skeptical that normally cautious European politicians would ever take the big step and implement monetary union. Indeed, the leaders who pushed Europe to the point of no return, German Chancellor Helmut Kohl and the late President François Mitterrand, were only dimly aware of the economic and financial whirlwind they were stirring up.

Europe’s politicians are moving forward for three reasons. First, few Continental European leaders have been able to push through economic reforms by appealing directly to voters. Yet Europe’s largest employers have shown

that without dramatic change, they will keep shipping jobs offshore. For reformers, the euro has become a backdoor approach to imposing the pain needed to renew Europe. Neither voters nor special interests will see its effects until it’s too late. The euro is “a Trojan horse,” says David Bower, European equity strategist for Merrill Lynch & Co.

Many gains have been banked already. The campaign to join the euro club helped governments do what they had to do anyway—curb spending against the demands of union politicians, and subsidized companies.

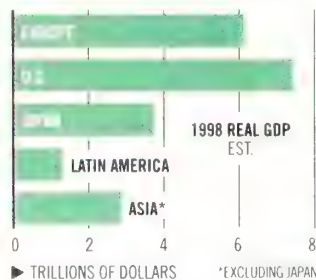
Finally, even reluctant politicians recognize that business confidence is up. The euro campaign has helped kick off more growth than Europe has seen in nearly a decade. Mergers to streamline companies jumped 48% last year. \$384 billion, and a new culture of shareholder value is seeping into executive suites.

But there are bumps ahead that could hurt the euro’s momentum, or even derail it. The currency system officially starts on Jan. 1, 1999, when corporate books, bank transfers, credit-card payments, and even home mortgages can begin to be figured in euros (table). The European Central Bank will also begin setting interest rates. Euro coins and notes must start changing hands on Jan. 1, 2002. Just the mechanics of making the system work is likely to cause shocks. A strong economy could cushion the blows. But if a recession hits Europe,

PORTRAIT OF A CHANGING EUROPE

The New Economy

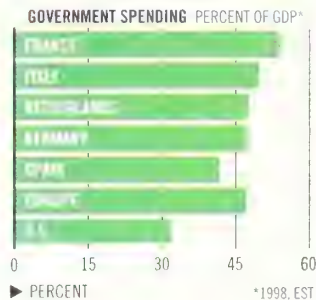
IT'S ONE OF THE WORLD'S LARGEST...



...GROWTH IS STARTING TO PICK UP...



...BUT GOVERNMENT IS TOO BIG...

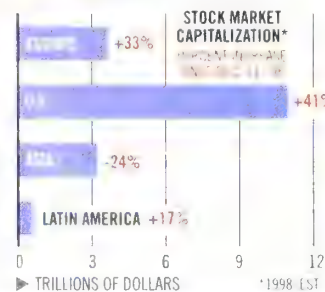


...AND JOBS REMAIN SCARCE

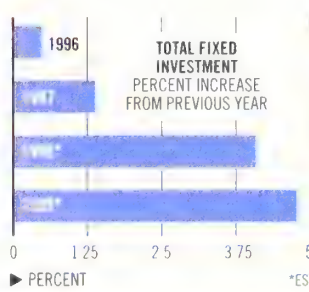


The Corporation

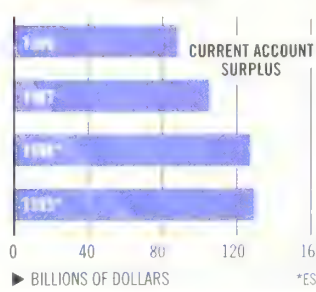
COMPANIES ARE GROWING RICHER...



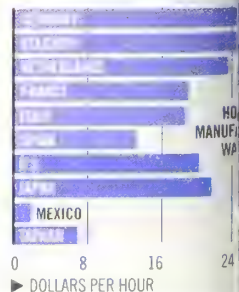
...THEY'RE INVESTING MORE...



...EXPORTING MORE...



...AND TRYING TO CURB COSTS



, the euro will be blamed and politi-
s will run for cover.
ill, the real measure of the euro's
power will be how much deep-seat-
economic reform it triggers across
Continent. There are formidable
ahead. As restructuring hits and
employment rises, politicians will
be under intense pressure to raise
ding and taxes. But that old ap-
ch will deepen problems in the euro
High-tax economies are likely to
ten, while lower-tax players would

Many workers will also suffer. If,
example, Spain slumps, will its workers move to Ger-
y to find jobs? The answer now is no—unless govern-
s agree to standardize job requirements and pensions.
the workers' part, old habits die hard. It seems likely,
ever, that if French socialists hold to a 35-hour work-
while Portugal allows longer hours, companies will
the south to save costs, just as U.S. companies shunted
from New York to Texas—and now, to Mexico.

TERED BANKS. Massive job disruptions are almost a cer-
y. By most estimates, one in five workers will be af-
d by mergers and downsizing, and some 5% of em-
ees could lose their jobs. Even at the peak of America's
sizing and Britain's Thatcher revolution in the early
s, job turmoil was not greater than these levels. Take
s. Analysts estimate that as many as a half of the
00 bank branches across the Continent may have to

EURO COUNTDOWN

MAY 2-3, 1998 Govern-
ments pick EMU mem-
bers and set exchange
rates for entry.

JAN. 1, 1999 European
Central Bank takes over
monetary policy. Nation-
al currencies remain, but

stocks and government
debt will be de-
nominated in euros.
Bank accounts, credit
cards, and prices begin
to be measured in euros.

JAN. 1, 2002 Euro physi-
cally begins to replace

national currencies.
Retail payments allowed
only in euros.

JULY 1, 2002 National cur-
rencies cease to exist,
replaced by euros.

DATA: BANQUE PARIBAS;
EUROPEAN COMMISSION

close. Tens of thousands of workers in these banks could be
early casualties of the euro.

No government could withstand a siege like this. Eu-
rope probably won't have to, either. That's because job cut-
backs will stretch out for years, even as new jobs—tempo-
rary and full-time—are created in small companies and
service businesses. The underground economy will also ab-
sorb the shock. An estimated 28 million people, or nearly one
in five workers, work
off the books.

But the key to the
euro's success has to be
growth. Much of the re-
structuring now gripping Europe is a result of deregulation
as companies get ready to meet global competition. They are
laying a foundation for economic expansion. In deregulated in-
dustries such as telecoms and airlines, new players are com-
ing in. As larger companies retool and shift to faster-growth
areas, new service companies are springing up around them.
These are providing new jobs—but often at less pay. The
Netherlands has pushed unemployment down to 5.2% from
Europe's average 11% rate by deregulating, holding the line
on wages, and encouraging flexible employment.

Perhaps the greatest pro-growth effect of the euro will
come as it spurs price competition. As prices become visible
in one currency across the Continent, costs will be instantly
comparable. Companies will reallocate investment to the
most profitable regions. While jobs will be lost, more Euro-
pean companies should be able to compete globally. Says
Louis R. Hughes, president of General Motors Corp.'s in-
ternational operations: "Whether in two, three, or five years,
Europe will be a lot leaner and more competitive."

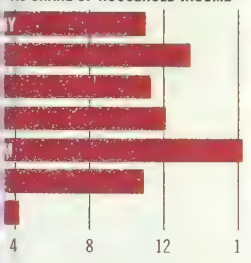
The new competitiveness could be further sharpened as
Europe's governments start comparing tax and spending
rates. High business taxes will become increasingly difficult
for governments to maintain once monetary union is in full
operation. Finland's top corporate tax rate, for example, is
just 27%, vs. 57% for Germany. Once the euro is in place,
governments will no longer be able to devalue to lower
costs, so companies will have to move. "If you remove cur-
rency as a safety valve, governments will be forced to focus
on real changes to become more competitive: lower taxes, la-
bor-market flexibility, and a more favorable regulatory back-
drop for business," says Ravi Bulchandani, a Morgan Stanley
Dean Witter & Co. economist in London. If that happens, an-
alysts figure euro club economies could expand an average
3% or more annually over the next decade.

Foreign investors, led by finance companies, will also
spur jobs and growth. Investment banks such as Morgan
Stanley, Goldman Sachs, and Merrill Lynch are shifting peo-
ple from New York to London to exploit EMU's possibilities.
The lure: a giant new financial market. For starters, the euro
zone government bond market—at \$1.9 trillion and almost as
big as the U.S. Treasury market—is apt to diversify. That's

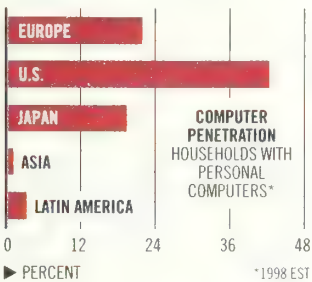
The People

EUROPEANS ARE BIG SAVERS...

AS SHARE OF HOUSEHOLD INCOME



...BUT TECH SPENDING LAGS



EW ECONOMY) GOLDMAN, SACHS & CO.; INTER-AMERICAN DEVELOPMENT BANK, MORGAN STANLEY,
VANTY; J.P. MORGAN & CO.; GOLDMAN, SACHS & CO.; (THE PEOPLE) INTERNATIONAL DATA CORP.; HSBC
ECD; (THE CORPORATION) MORGAN STANLEY, INTERNATIONAL FINANCE CORP.; GOLDMAN, SACHS & CO.;
"GOD'S DRI

Special Report

THE EURO



because strapped central governments, which generally have done most of the borrowing, are expected to push spending onto municipalities.

On top of that, the corporate bond market in the euro zone is valued at just \$160 billion, one-sixth the size of the U.S.'s. And its stock markets have a combined capitalization of just \$3.6 trillion, less than one-third the size of U.S. equity markets. Goldman, Sachs & Co. figures the corporate bond market will quadruple in size, to \$800 billion. Fragmented Continental equity markets also are likely to merge.

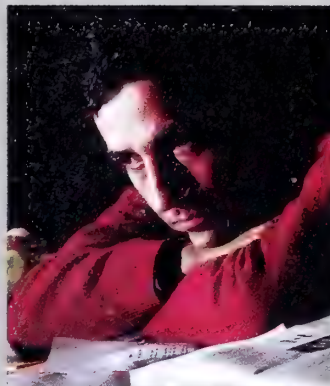
FLEXIBLE WORKERS. The prospect of cheaper money and shareholder demands for higher performance are also changing corporate Europe. Underperforming conglomerates have been selling units that can't match rivals' profits. Siemens last year spun off its dental-products unit into a leveraged buyout, a company called Sirona. Alcatel Alsthom in France and Philips Electronics in the Netherlands have been paring down, too. As a result, companies are investing in winners—not losers.

Amid this restructuring, one point has

been obscured: Workers are grudgingly becoming more flexible. From Daimler Benz to tiny knitting-needle maker Gustav Selzer, for example, German companies are negotiating plant-by-plant pay and work-rule concessions they couldn't before. That's one reason unit labor costs in Europe will rise just 0.7% this year, Germany's will probably fall by 0.5%, after dropping 1.7% last year.

As the euro kicks in, it's also likely to speed deregulation, which has already reordered Europe's corporate landscape. Since the European Union mandated deregulation of airlines last year and of telecoms as of last January, upstart challengers have been taking on national giants such as air carrier Alitalia and Deutsche Telekom. Now, Germany says it will totally open its postal market by 2003. Klaus Zumwinkel, the ex-head of mail-order giant Quelle who now is CEO of Deutsche Post, says he will be

V
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SKEPTIC:

"Monetary union is a crazy project. It creates deflation. That's why the currency will be a disaster."

—Emmanuel Todd, French Philosopher

ready. "In the real world, things are going to happen much faster than politicians expect," he contends.

Indeed, some European investors are talking about a "golden" scenario for the Continent. In this view, Europe will take on attributes of the American "New Economy," with high productivity, low inflation, and steady growth. If Europe becomes an expanding economic power, it will have gained the wherewithal to pursue its own global political agenda. Cementing European economic union will inevitably lead to talk of greater political integration.

The big question is how European citizens themselves will react to all this. Europe's elites have promised average citizens that the new Europe will be able to hold its own against the best in the global marketplace and create jobs. What they have left unsaid is that in this new era, Europeans will face a more economically insecure future, without social protections they have enjoyed until now.

But optimists believe the politicians are unleashing a process that will mean major progress. "The market tends to push things much faster than regulators expect," says Mark Frevert, head of European operations of U.S. energy giant Enron Corp. That's perhaps more prosaic than the rebuilding that led European visionaries to dream of a common currency 40 years ago. But if it works in this age of global markets, it could prove to be just as significant.

By Thane Peterson in Frankfurt

Special Report

THE EURO

THE EURO COULD REMAKE EUROPE...

COMPANIES

Consolidation in manufacturing will accelerate as companies merge, close plants, and reorganize distribution. Service industries could boom.

FINANCE

Continental stock markets will grow larger, partly by merging. Corporate and junk-bond markets will boom. Low-profit banks will be takeover bait.

LABOR

As capital becomes more mobile, labor will be on the defensive. Unemployment may fall as jobs are created, but wages will be under pressure.

CONSUMERS

Consumers will get a better break. Price differentials will narrow, and cheap imports from Asia and Central Europe will become more plentiful.

TAXES

Pressure from lower-tax countries may finally force Germany and France to reform tax systems and pare back government.

...BUT NOT WITHOUT DISLOCATION

POLITICAL TENSIONS

In a downturn, European countries will diverge over monetary policy. Major battles could erupt over tax policies and subsidies to poorer EMU nations.

INCOME INEQUALITY

EMU budget deficit rules may force cuts in health and welfare benefits. The gap between rich and poor may expand.

BOOM AND BUST

Forced to adopt low interest rates, fast-growing countries such as Ireland may suffer from overheating and a bust in property and stock markets.

GLOBAL COMPETITION

As Europe attracts foreign rivals, homegrown companies will be under pressure to invest in lower-cost Central Europe or Asia.

LOSS OF STYLE

The EMU will speed the closing of small shops, and expansion of chain eateries and discount stores, that could diminish local character.



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count on the weather,
MCI makes sure
you can count on
The Weather Channel®
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The Great Money Bazaar

The EMU has altered the landscape for good

In Europe's new economy, finance is Ground Zero, the starting point for the virtuous circle that Europe's planners intended to set in motion with monetary union. For the first time, the Continent has a monetary glue that, if it holds, will force its economies to become more efficient, however painful that might be.

Even before a single euro coin is circulated, the prospect of monetary union is transforming Europe's financial scene. Cautious German and Italian investors, who formerly wouldn't put their savings into anything riskier than their own government's bonds, now have an appetite for British Telecom equity warrants and Polish debt. Banks are feeding their hunger with new products and services, from mutual funds to magazines. Companies are financing takeovers and U.S.-style management buyouts by issuing their first-ever junk bonds and cleaning up their reporting to prove the bonds are safe.

Indeed, after Europe's capital markets switch to the single currency on Jan. 1, they will instantly acquire more muscle and longer reach. The euro will wipe out some \$65 billion annually in currency exchange costs and cut the middleman out of trillions of dollars' worth of transactions. Making Europe's monies one will create a vast pool

of capital that is suddenly far more mobile than before. Overnight, 11 separate government bond markets will turn into a single, \$2 trillion behemoth. Italy's paltry \$68 billion stock market has the potential to balloon to \$275 billion. The Continent's corporate bond market could quadruple, to nearly \$800 billion. The hundreds of billions in low-earning government funds that now finance workers' retirement will give way to a new universe of fast-growing, privately managed pension assets. In the space of only a few years, the Europeans hope to fashion the sort of unified financial market it took Americans a century to establish.

FRONT LINES. These huge financial markets will reshape Europe's corporations and modernize its economy. Without the traditional weapon of currency devaluation to patch over economic weakness, governments, companies, and banks will have to fight for capital. That means slashing costs and budget deficits, showing stable, predictable growth, and offering investors appealing returns.

An enlarged financial market also will attract more investors both inside and outside Europe. No longer able to trade on currency risk, these investors will seek yield in new places. Already, money is flooding into the fledgling small-cap markets, nurturing technology and biotech startups. Shareholders are demanding more from management at formerly complacent corporate giants, quickly rewarding those that

streamline and punishing the laggards.

Financial institutions are at the front lines of the fight for capital. To milk the nascent markets in asset management, trading, and underwriting, financial services firms are joining forces across national borders and investing in technology. With the state's role shrinking, they want to be the private handlers of Europe's savings and providers of its safety net. "We see the euro as a catalyst for a totally new approach to investing," says Bernd Maltzan, head of private banking at Deutsche Bank.

As governments cut spending to qualify for the EMU, interest rates have come down—to just 5% long-term and 3.5% to 4% for short rates. That is pushing more and more investors into stocks. And because Europe's equity markets have so much room to grow, the 34.8% average rise



Special Report

THE EURO

European bourses since January, 1997, will be just the beginning.

The forces that started the equity boom could keep driving it for at least a few more years. First, interest rates are expected to stay low. Inflation is nowhere near the horizon in Europe's core economies, and EMU members have committed themselves to continued fiscal discipline post-euro.

Second, Europe's privatization wave will keep on rolling. Governments are keen to get money-losing businesses, such as banks to utilities, off their books. Morgan & Co. forecasts that European privatization offerings will total \$62 billion in 1998. Third, the merg-

er mania that has swept the region in the past several years will grow wilder as companies try to build European muscle. That will expand the tier of transnational giants for investors—Europe's new blue chips.

Low interest rates and lots of new stock opportunities bode well for the equity markets.

But they won't all boom together. The reason is that investors will increasingly benchmark their returns against European-wide indexes, such as the Dow Jones Euro STOXX 50 or FTSE's Eurotop 100. To match the indexes' performance, they'll need to shift out of domestic markets toward top European equities.

Instead of automatically buying French retailer Carrefour, for instance, a French investor will be more likely to look at Britain's Marks & Spencer PLC. German investors are already shunning popular Deutsche Telekom for faster-growing challengers. And old-style conglomerates, from Hoechst in chemicals to Italy's state-owned IRI in energy, will wind up losers unless they spin off their marginal units and form alliances with strong partners in their core business.

The Continent's new, return-hungry stock buyers will shed a stark light on competitive failings. The need to differentiate out of home markets is forcing investors to think globally, measuring European players against U.S. industry peers. "Siemens can't behave very differently from General Electric," says one German money manager. "Deutsche Bank to behave like the U.S. banks, and we have to worry about Fidelity and Vanguard."

SMORGASBORD. Investors' quest for returns will also translate into the gigantic new bond market. "The big story is the search for yield and diversification," says Ralf Schreyer, a manager at DWS, Deutsche Bank's mutual-fund arm. As a result, there will be an explosion in debt instruments offering investors a smorgasbord of new risk classes. For the time being, there's a ready market for state-backed municipal bonds, high-yield corporate debt, and everything in between. "The focus shifts from currency risk to credit risk,"

Alexander Schrader, head of economics at Bayerische Vereinsbank. "Everyone is looking for a bigger spread." Most analysts expect the lower-yielding government bond market to contract, at least initially. To stick with the EMU program, its members have to contract debt. They also have to keep lower budget deficits, so interest rates aren't likely to diverge much. Some portfolio managers are now buying Greek debt, yielding 350 basis points more than U.S. Treasuries, on the theory that Greece will join the EMU in 2001.

Bonds, bourses, and small-cap markets could boom; banks may well face a bloodbath

The bravest buyers are taking positions in high-yielding Czech and Polish bonds.

No wonder the EMU's core governments are trying to make their own bond markets more attractive. France is introducing new debt instruments such as inflation-indexed bonds. Other governments are standardizing the formulas by which they calculate interest or adopting fixed calendars for their debt auctions. Such changes all serve to make the government bond market more transparent and more liquid. "This is definitely increasing competitiveness in bonds," says Martin Brookes, international economist at Goldman Sachs & Co. in London.

Greater competition also creates a huge opportunity for companies to raise low-cost capital. One reason the European corporate bond market has remained so tiny is that there were too few investors to make corporate debt issues worthwhile. Thanks to legal restrictions on how much money investors could put into foreign currencies, a French company issuing a bond had to depend largely on French buyers. And issuing debt in German marks to attract German in-

EUROPE'S MARKETS WILL EXPLODE...

PRE-EMU

POST-EMU

11 national stock markets trading in local currencies with a \$2.5 trillion market capitalization

Fewer exchanges, with a euro-denominated market capitalization as high as \$7.5 trillion

11 separate government bond markets worth \$2 trillion

A single euro bond market that may increase by \$500 billion

An illiquid \$160 billion corporate debt market

An active \$800 billion corporate-debt market

Some \$650 billion worth of government pension liabilities

Steady flows into fast-growing, privately managed pension-fund assets

...GIVING INVESTORS A BRAND-NEW MENU

STOCK Local heroes such as Volkswagen will play second fiddle to trans-European giants such as SAP. Expect big cross-border takeover plays in banking and aerospace. Look for initial public offerings.

BONDS A smorgasbord of corporates will appear, from AAA-rated to junk. The high-yield corporate bond market could hit \$8 billion in this year. Even sovereign debt will pick up, with governments adding maturities.

NEW PRODUCTS A mutual fund for every wallet and risk tolerance. Next to plain-vanilla stock-index funds, look for sector funds, low-risk "retirement" funds, exotic country funds. Fees will keep coming down, too.

DATA BUSINESS WEEK

vestors was prohibitively expensive. Now, without the obstacle of currency risk, companies can peddle their debt throughout the EMU region.

In addition, startups have a new advantage. As banks get out of the lending business, big companies will issue safe, AAA-rated bonds paying one or two percentage points more than government debt. But more aggressive investors will be eager to lend to tiny new companies issuing riskier bonds. The market in European high-yield corporate debt grew from \$2 billion to \$4 billion in 1997

and could double again in 1998. The pattern is already showing in stocks, where Europe's

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small-cap Nouveau Marché and Neue Markt have risen three times faster than the broader markets this year.

There will be losers in Europe's financial free-for-all. And as the sellers of money, the banks have the most to fear. Not only will lenders lose big income as foreign exchange trading and money-market operations shrink in importance, but their margins will come under even greater pressure as the industry continues to consolidate. From France's loss-ridden Crédit Lyonnais to the smallest savings bank in Germany, the euro represents a watershed. It will take a heavy toll on their former bread-and-butter wholesale businesses, from government bond trading to foreign exchange. McKinsey & Co. estimates that together, such businesses account for 40% to 80% of European bank revenues.

TOOTH AND NAIL. Over the long term, banks must reinvent themselves to make the most of Europe's new capital markets. Their cozy lending relationships with industrial giants, bolstered by cross-shareholding and overlapping boards, will no longer be profitable. Instead, they need to beef up the much more lucrative areas of asset management, underwriting, and M&A. That's what drove Deutsche Bank, Dresdner Bank, and Swiss Bank Corp., for example, to buy British investment-banking houses. If Europe hones its expertise in investment banking, it could soon have its own class of superstars pulling down millions for taking a Continental version of Netscape public, for example.

But with U.S. rivals like Morgan Stanley Dean Witter & Co. and Merrill Lynch & Co. breathing down their necks—and in the face of huge new combos such as Citicorp and Travelers Group Inc.—Europeans also have to slash costs to compete. So the wave of mergers that created the \$25 billion UBS-SBC will crest into even more epic consolidation over the next decade. Many analysts think only 10 big banks will survive the shakeout. The efficient Dutch and market-savvy British and Swiss look like winners. The French and Germans get few votes of confidence.

As the euro decimates old-line activities and creates new markets for

new products, banks are scrambling to create business lines from scratch, while fighting tooth and nail over traditional ones. They are selling insurance and mutual funds in each other's territory and racing to be first to market with new-fangled products such as structured debt portfolios aimed at hedge funds. The biggest lenders are sparing over whose brand name will grace the new, Europe-wide stock indexes and who will come up with a Moody's-style rating system for European corporate bonds.

In overbanked France, Germany, and Italy, the bloodbath has barely begun. Half of the Continent's bank branches—and hundreds of thousands of jobs—need to be eliminated before these countries' banks are in fighting trim to compete in a borderless Europe. With returns on equity averaging 9%, compared with 17% for U.S. competitors, Europe's banks lag far behind its manufacturing companies in much-needed downsizing.

The same fierce competition driving bank consolidation is raging among another keeper of Europe's finance infrastructure—the exchanges. The euro will render obsolete much of the trading in bond-based contracts that makes up the exchanges' core earnings. Some exchanges will just disappear. The common market has 32 stock exchanges, compared with eight in the U.S., and 23 derivatives exchanges, versus seven in the U.S. Over the next 10 years, euro business is likely to concentrate in three or four huge, efficient centers that trade the most popular products and give members access to others around the world.

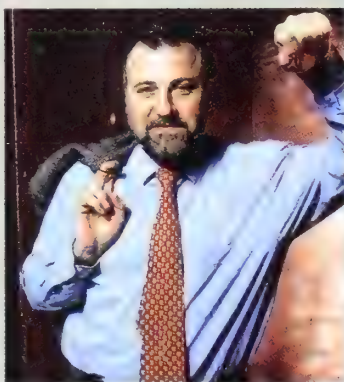
In preparation, European exchanges are computerizing—and challenging the once dominant London International Financial Futures & Options Exchange, which still uses the open-outcry system, in the process. France's Matif SA, Europe's third-largest derivatives exchange, launched computerized trading on Apr. 7 after a strike by open-outcry traders fearful of losing their jobs.

Frankfurt's computerized Deutsche Terminbörse (DTB) has snared 70% of European trading in Bund futures, up from a 30% market share a year ago, all at LIFFE's expense. "The future of trading bond futures contracts is on a screen," admits Guy Simpkin, director of product development for LIFFE. His exchange has announced a schedule for going electronic—an investment of \$33 million to \$66 million. On the defensive, it has also announced an ownership restructuring intended to focus more closely on profitability.

Companies and investors will be the big beneficiaries of such efforts. That was the whole idea behind the new Europe, after all. Just as mass production brought down the price of goods for consumers, the EMU is lowering the price of money, creating more resources for innovation and wealth. Even if monetary union isn't a smash hit, the changes it has already wrought in Europe's financial markets are likely to have a healthy and long-lasting effect.

By Joan Warner in Frankfurt

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WORRIED:

"One important thing Germans are proud of is the Deutschemark. It has a psychological value for Germans. We must now give up this thing that we are so proud of. It's emotional. People don't sense the advantages."

— Klaus Wiesehügel, chairman of German construction workers' union



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CORPORATIONS

Industrial Evolution

Coming soon: A leaner Corporate Europe

Jean-Pierre Rodier, CEO of French aluminum giant Pechiney, is racing to create the new European corporation. When he arrived in 1994, Pechiney was a lumbering state-owned dinosaur, suffocated by high costs, an enormous debt load, and a lack of focus. Four years later, his company is lean, privatized, and profitable. "That was the easy part," says Rodier. Like other corporate brass, he believes that Europe, newly welded together by a common

currency, faces a five-year stretch of intense competition as companies slash prices, trim suppliers, and make

"major changes in production methods."

Europe's industry is about to get a radical face-lift as the euro upsets the status quo. The common currency will immediately highlight pricing disparities, helping strong companies to snatch markets. The resulting squeeze on profit margins will force Corporate Europe to seek economies of scale as never before in a torrent of mergers

and plant shutdowns. With currency risks gone, companies won't need to operate in as many countries as today. Many are already preparing to move to fewer, cheaper locales.

MERCEDES PLANT

Manufacturing will be more competitive and more profitable

As change cascades through Corporate Europe, one in five workers may have to change jobs over the next five years. That will increase the chances of a political backlash. Industry will scatter as much production as it can to the south and east of Europe, where labor costs and taxes are lower. Manufacturing, though it will make up a lesser share of the economy, will be globally competitive and much more profitable.

Many analysts believe that a tougher, feistier Europe will emerge from the turmoil. Overall, costs will fall and governments will come under pressure to slash taxes to save jobs. The optimistic view is that Europe's business climate will be much more hospitable to growth industries. Entrepreneurs and venture capitalists believe that a re-invigorated Europe will better nurture Information-Age products, from the Internet to computers-on-a-chip, along with biotech goods and services. Small and midsize companies will produce more of Europe's output. "The euro is going to help create sustained European growth" of 3% or 4% a year, says Jean-Marie Messier, CEO of France's Compagnie Générale des Eaux.

COMPARE AND SAVE. The process isn't alchemy; it's simply a matter of letting the markets work at last. The euro is the catalyst because of the added power it gives Europe's new financial markets. National governments will no longer be able to rig bond markets in their favor, so they won't be able to run up huge deficits with impunity. European Union antitrust cops are also compelling governments to scale back huge subsidies to erstwhile national champions such as Crédit Lyonnais. And as Europe's banks feel the heat of competition, they will start to un-

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bad industrial holdings, blowing away the cobwebs of corporate cross-shareholdings. Companies will be in open competition for capital and credit. "The result will be [a fiercely competitive] business environment which Europe has spent the last 50 years trying to avoid," says Jonathan Story, professor at France's INSEAD management school near Paris.

Pricing will be a potent agent of change. Starting next year, it will be a snap for Europeans from Lisbon to Copenhagen to compare prices on everything from refrigerators to heavy machinery, because they'll all be quoted in the same money. So-called pricing transparency is an obvious boon to consumers and corporate purchasing departments. But it will be a curse to uncompetitive companies or those that have been able to stick national markets for whatever they would bear. "The lack of a single currency was one of many invisible barriers," says Serge Foucher, chief financial officer at Sony Europe.

Drugmakers are masters of this game. Drug prices can vary as much as 250% between the rich socialized medical systems of Northern Europe and the poorer ones in the south. "We will meet in the middle [of the price range]," says a confident John Manser, head of group treasury at Swiss drug giant Novartis. Many consultants disagree, predicting prices will tumble, squeezing profits. "It is a time bomb," says Kamran Kashani, marketing professor at Lausanne's IMD business school.

MERGER MANIA. The cleansing action of Continentwide price competition will prompt big changes. "The market will force companies to do things that they didn't have to do in the past," says Jimm Dunn, director of the euro program at General Motors Europe in London.

What's alarming is that thousands of European managers don't yet understand this. Most, says François Harrière, a partner at Andersen Consulting in Paris, view the euro as a bookkeeping issue and are not ready for the coming blast of competition. "The real problem is not whether you can invoice in euros within two years. It is whether you will have any customers left," he says.

On the brighter side, the euro will help bring down costs. Companies will save on foreign currency exchange and hedging costs—\$55 million a year at Germany's giant autos-to-aerospace group Daimler Benz alone. Europewide, savings could reach \$65 billion a year.

But even that is penny-ante stuff alongside massive cost-cutting through economies of scale. Europe's chief executives will be able as never before to streamline operations. They are already taking the scalpel to production sites, supplier networks, and warehousing. With currency risks gone, the whole of Europe becomes one giant home market.

Global competition pushed companies to start restructuring. Now, the euro will force the pace. French remaker Michelin, for example, is closing 90% of its European distribution centers, relying on 20 instead of 200. Japan's Toyota Motor Corp. is raking over all its local plants with a view to scaling back. Leaner marketing will help, too. Daimler, for instance, will organize sales and service—as well as finance and leasing—into bigger regional operations. "The impact will be

HOW THE MARKETS ARE BETTING ON THE NEW EUROPE

*How professionals may switch investments**

WINNERS	BILLIONS OF DOLLARS	LOSERS	BILLIONS OF DOLLARS
Energy	+6.7	Banks, insurance	-7.0
Financial services	+3.2	Chemicals, pharma	-2.8
Construction	+3.1	Media	-2.7
Tech, Telecoms	+2.7	Food	-2.1
Retailers	+1.7	Conglomerates	-1.2

*Projected over 18 months

DATA: DEUTSCHE MORGAN GRENELL INC.

colossal," says Christian Saint-Etienne, an economics professor at the University of Paris.

The changes are sparking a European merger boom. Last year, a record \$384 billion of deals were done involving 5,250 companies. The process will help reshape Europe's industrial map. Initially, high-cost countries such as Germany and France will tend to hemorrhage, while low wages and taxes in others such as Spain and Ireland will attract foreign investment. Spain is already booming, with inflows up 23%, to \$17 billion, last year. New arrivals include Swedish telephone-equipment maker L. M. Ericsson and South Korean electronics giant Daewoo.

As companies vote with their feet, politicians will come under severe pressure to slash taxes and social charges and loosen up inflexible labor markets. So corporate migration may lead Europe to standardize taxes, social laws, and labor rules. Although national politicians will fight to hang on to power over these social levers, their grip is likely to slip. "Price transparency will certainly let people see more clearly where there are distortions in the marketplace," says Unilever PLC chairman Niall FitzGerald.

Such pressures might help blow away one of Europe's most anticompetitive habits—propping up inefficient old-line industries because they're big employers. Finally, Europe could get a much stronger economy. But only if politicians don't panic and try to resist market forces when the early going gets rough. "The good news is that it's short-term destruction," says Michael Kraland, partner at Parisian investment advisers Trinity Capital Partners.

To succeed, many economists say, the euro needs a period of high European growth. But with a bit of luck—and providing they don't flinch—Europe's leaders may be on the brink of pulling off the Continent's boldest economic project since World War II.

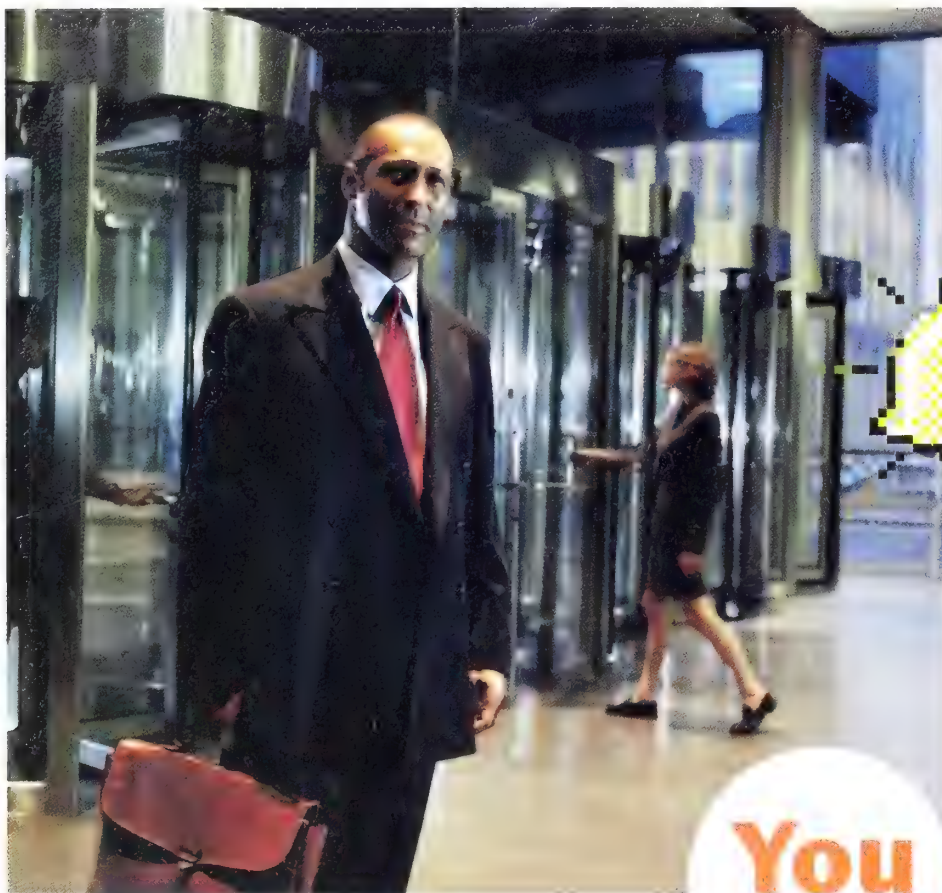
By Gail Edmondson in Paris, with bureau reports

GETTING READY

"A strong euro . . . would be great for exports. If it becomes a reserve currency, that would be even better. It would mean more foreign direct investment in the Czech Republic. If we clean up our economy, foreign companies will definitely come in."

—Michal Tomasek, 35, economist and European Union adviser to Komerční Bank





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Sent: Friday, 6:15 p.m.
To: Anyone still at work
Re: Go home.

We can't guarantee you a 9-to-5 life. But if you're working hours straight out of a Dickens novel, [Microsoft® Office 97](http://www.microsoft.com/office/) can help slice time off your workday with smart tools that let you get more done with less effort. For example, Microsoft Word keeps a wary eye on your typing, correcting spelling and grammar flubs on the fly...and can automatically finish typing dates and common words. AutoCorrect in Microsoft Excel can correct common formula errors as you go. Keep everything organized in one place with the Outlook™ desktop information manager. Turn the Internet into your source of instant answers. And if you hit a wall, ask our Office Assistant a simple question and you'll get a simple answer. With Office 97, you're as productive as you ever were. You may just get home earlier. So while you're still at the office, check out Office 97 at www.microsoft.com/office/.

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COMMENTARY

By Stephen Baker

'A Major Rebirth'?

In technology, Europe is out to finally forge a role as a global leader

Europe has a long tradition as an obstacle course for entrepreneurs. From Hasso Plattner's industrial-software concern to Pierre Chambon's biotech startup, Transgene, technology companies have faced a risk-averse culture, a morass of regulation, and a dearth of capital. So it hasn't been surprising to see Europe fall far behind the U.S. "We missed a few steps," concedes Plattner, co-founder and co-chairman of \$3.5 billion German software giant SAP.

But if the forces sweeping Europe, from the euro to the Net, succeed in lifting its lackluster economy toward its potential, could the region take its place as a global technology leader? If so, in which industries will it shine? **SOLID PRESENCE.** Success is no given, but Europe certainly has a chance. The main reason is that over the past 10 years, European companies have built a solid presence in three technologies likely to see huge growth: wireless communications, business software, and biotechnology. To go further, Europe must hold on to its talent and channel capital intelligently. William A. Etherington, IBM's general manager in Europe, is among the optimists. "Europe is on the threshold of a major rebirth," he says.

The region is already ahead in wireless communications. L. M. Ericsson and Nokia are turning

Scandinavia into a wireless society. The trend is catching on in Spain, where Telefónica sees the mobile-phone market rising 100% a year. Growth in European cellular subscribers is 56% yearly—15% higher than the world average. Unlike the U.S., Europe has one standard—and will soon be a united market of 300 million consumers.

Deregulation ushered in Scandinavia's wireless breakthrough. But even in more hostile terrain, the old obstacles have fostered creativity. From its start in the country town of Walldorf in 1992, SAP has become Europe's answer to Microsoft Corp. SAP's "enterprise" systems put all corporate information—from inventory in Singapore to accounts payable in Newark—at the CEO's fingertips. SAP's sales have quadrupled in five years, and its market cap is second to Microsoft's in the industry. Its next goal is to

connect a company's system to those of customers and suppliers.

SAP is hardly alone. Europeans are designing advanced systems for everything from data mining to online banking. Belgium's Lernout & Hauspie Speech Products is a global contender in speech-recognition software, key to talking E-mail. L&H has headquarters in Brussels and Boston, and Microsoft bought 15% of its stock last year. The drift is clear: Europe's tech economy is melding with America's as its companies benchmark against U.S. players.

Successes against global rivals have helped European software startups gain access to financial markets once closed to them. Venture capital is pouring in, priming the pump for new issues on the NASDAQ and six high-tech markets across Europe. At Frankfurt's 21-company

Neue Markt, total market capitalization doubled, to \$11.5 billion, in the first three months of this year.

Access to capital has proved just as critical to European biotech. University-bred startups in Cambridge, Munich, and Paris have cutting-edge technology in genomics and anticancer compounds. Initial public offerings are on the rise. In April, France's Transgene was oversubscribed when it listed on NASDAQ. Europe is luring financiers worried that the U.S., with seven times as many biotech listings, may be saturated.

But Europe won't lead in tech without talent. A brain drain has hit hard in France, where taxes have pushed entrepreneurs out. While rules are easing, the market is more likely to make the difference. A common currency will show which countries reward wealth generation—or punish it. Rivalry for jobs and capital may engender a friendlier investor climate and reverse the talent drift.

The transformation from high-tech laggard to digital star is clearly a work in progress. But the Continent has come far in a short time. A decade ago, Americans with modems hid them from customs officials in Europe's protected monopolies. Now, Europe is poised to join the world's high-tech leaders—to shine from cell phones to biotech and beyond.

Baker covers European technology from BUSINESS WEEK's Paris bureau.



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THE EURO



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[illegible]



LABOR

Workplace Earthquake?

Many will lose before gains kick in

A tumultuous era has begun for European labor. Industrial workers will have to surrender their dreams of secure, well-paid lifetime jobs as the euro forces European companies to restructure. Unemployment will soar: By some estimates, 2 million workers, or 5% of the industrial workforce, could be on the streets within 18 months. The whirlwind will hit Germany and France, where wages are highest and labor rules are the most rigid, with the most force. It could even spark a social explosion as angry workers fight change with strikes or votes for extremist political parties.

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may brim with jobs in small companies and services. Unions will play a smaller role, and sky-high social security levies will fall as countries vie to attract jobs.

Small countries are blazing the trail. In the 1980s, Dutch unions agreed to cut wages and ease work rules, trading fewer permanent full-time jobs for more temporary and part-time ones. Now, Dutch unemployment is just 5.2%, or around half of Europe's 11% rate.

But the sculpting needed to carve out a new labor market is monumental. After a painful decade in the U.S., just 1 employee in 4 works in manufacturing, vs. 4 out of 10 in Germany. Some 25% of Americans now work in shops, hotels, and restaurants, vs. 15% in Germany.

But after the storm, Europe's sclerotic labor scene could be transformed. In a decade, the Continent

Deregulation and competition are closing that gap in some countries. For example, Federal Express Corp. has added 1,700 jobs in Europe over the past five years. And McDonald's Corp. is opening two outlets every three days. Altogether, Europe has added a million service jobs in the past five years.

But many Europeans still sniff at low-paying service posts. When Warner Bros. Inc. wanted to hire 1,100 people for a theme park in the Ruhr Valley in 1996, its recruiters weren't greeted as heroes. Instead, Sabine Burzler, a local official charged with placing jobless miners, told them: "You offer bad jobs: poorly paid seasonal work. Plus, you insist that the workers always smile!"

Europe's labor bosses certainly aren't smiling. They fear that euro hype camouflages a deadly effort to create a two-tiered labor market in which only a small elite has good, permanent positions while the rest have insecure, low-wage jobs or work off the books.

As inequality, black-market jobs, and unemployment grow, unions are on the defensive. "Business will be tempted to use its new power to kill unions," says Barbara Gerstenberger of the Brussels-based European Metalworkers Union. Union attempts to slow layoffs by lobbying the EU to impose a single set of European work and social-security rules has flopped. Multinationals must set up Europewide management-labor councils—but they need meet only once a year and are purely consultative.

While business is freer than ever to cross borders, workers remain divided by culture, language, and benefit systems. Europeans can, of course, seek work anywhere in the EU. But few do, so the cure for unemployment will have to be found within national frontiers. Austrian and Belgian unions are starting to make concessions. Italy has rolled back controls on temps, while militant public-sector unions in Germany have settled for raises of 1.5%, a third of what they sought.

Still, there's risk of a backlash. Recent attacks by French jobless on unemployment offices in Paris offer a glimpse of what happens when workers' patience wears thin. Eventually, the euro should deliver faster growth and better-paying jobs. But the wait could be killing.

By William Echikson in Liège

FRENCH STRIKERS

Political and social turmoil could still derail reform



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COMMENTARY

By Joan Warner

'Mix Us Culturally? It's Impossible.'

For many Europeans, monetary union is an affront to their way of life

In the lush resort of Baden-Baden in southwestern Germany, Brigitte and Heide Hönes run a tiny hilltop hotel inherited from their parents in 1957. A prewar sanatorium, the Hotel Tanneck still caters to tourists taking the town's thermal waters. But business is off since the government cut health benefits that covered a spa vacation every six years. And the Höneses don't think the euro will solve their problems. "We already have the strongest currency in Europe," says Brigitte.

Like many Europeans, the Höneses are being dragged into monetary union much against their will.

They don't buy the notion that EMU will boost growth and create jobs. Economists may say it's time for Europe to adopt U.S.-style capitalism. But the citizens of the new Europe aren't going to do it without a struggle.

So far, all they see are layoffs and social-spending cuts. Even more fundamental than the impact of these developments is what they stand for. To many Europeans, the coming of the euro has already begun eroding what the average European considers a civilized life. They see a single currency as an assault on values they hold dearer than unending growth, ever-higher stock prices, and the other yardsticks of what many Americans call the New Economy. In their view, the euro is not only an attack on the welfare state but also a threat to the old European idea of solidarity—the shared sense of community of which the welfare state is an expression.

Their resistance won't stop the euro—not with so much



only the euro but also neighbors. "The euro will increase political animosity and division," says Antonio Martino, economics professor at Rome's Free University. "It's the ideal way to pit one country against another."

Ordinary Europeans call Chancellor Helmut Kohl's vision of a politically united Europe delusional. "Maybe in 500 years," says Brigitte Hönes. "Kohl is crazy," asserts Hans-Peter Kratz, a Frankfurt cabbie, who is sure the euro will eventually cause inflation because of budgetary tricks leaders played to qualify for EMU. "He wants to destroy the small countries of Europe and mix us all together. But mix us culturally? It's impossible."

The U.S. is often held up to Europeans as an example of the clout a huge economy with one currency can realize. But while a single language and culture make it easy for a Wal-Mart or Barnes & Noble to conquer all of America, Europe has more evident limits to standardization, based on centuries of tradition. Cost-efficient supermarkets offering branded bread haven't wiped out local bakeries that sell fresh *baguettes* to the French and *Brötchen* to the Germans. And along with such personal preferences go deep political differences. France's statist tradition has already put it at odds with the rest of Europe in the drive to privatize. France has also shown a historically different approach to immigrants from its neighbors, insisting on assimilation

SKEPTICAL SISTERS

Real union would take 500 years, the Höneses say

rather than encouraging new ethnic communities. That could cause problems as more Europeans cross national borders in search of jobs.

"INERTIA." But the first backlash could come when Europeans come face-to-face with EMU. Britons still talk about the difficulty of changing to a decimal pound in 1971, and older French people still think in terms of *anciens francs*. "Money is like language—there's a great deal of inertia," says Martino. "Creating a new currency would be a risk under any circumstances. It is an enormous risk when that new currency is introduced against the will of the people who are going to use it."

Monetary union has survived many obstacles, from the skepticism of Europe's trading partners to the policies of its left-wing politicians. But the biggest challenge will come from the people who must soon stuff it in their wallets with such distrust and reluctance.

Special Report

THE EURO

leaders try to integrate Europe politically, there could be a government-topping backlash. Voters are already unhappy: In a recent German poll, 32% of respondents said monetary union should be postponed—and 33% said the euro shouldn't be introduced.

One danger in monetary union has been the extraordinary lack of communication between the leaders who conceived of it and the people who must live with it. "In Germany there has been no public debate," says Martin Hüfner, chief economist at Bayerische Vereinsbank. "The government didn't want it."

A bigger risk is greater nationalism. In France's local elections last month, the anti-EMU National Front won surprising margins. If inflation spikes in Italy or austerity brings about a recession in France, voters will blame not

Senior News Editor Warner covers Europe from Frankfurt.



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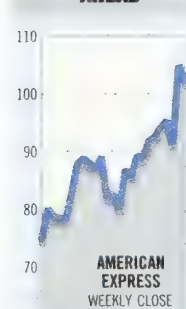
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BY GENE G. MARCIAL

ROMANCE FOR AMEX AND AIG?

In February, investment manager Robin Manners West stuck her neck out to tell this column that one bank she was sure would be taken over was First Chicago NBD, the nation's ninth-largest, and that Banc One would acquire it. Bingo!

CHARGING AHEAD



DATA: BLOOMBERG FINANCIAL MARKETS

On Apr. 13, First Chicago and Banc One announced they were merging, creating the No. 2 credit-card company. No. 1 is Citicorp, now uniting with Travelers Group.

What does all this signify? Plenty for American Express (AMEX)—best known for its charge-card and travel services—and for American International Group (AIG), says West, who manages \$1.8 billion for the New Mexico State Investment Council.

"AmEx had better do something to battle these new credit-card powerhouses," she argues. Ditto, she adds, for AIG, one of the largest holdings in her portfolio. Unless it moves quickly, says West, this insurance colossus will be overtaken by Citigroup (Citicorp-Travelers) as the world's largest financial-services company—in terms of market capitalization. What will AIG need to compete against Citigroup?

The answer, says West, is an AIG-AmEx merger, which she thinks they may be considering. Is such a deal doable? "After the recent round of mergers and takeovers, anything is possible," asserts Wayne Nordberg, chief of equity investing at Lord Abbett. He says more marriages lie ahead in the financial-services industry.

"AIG and AmEx will really need each other now, and there is no overlap in operations, except a tad in the financial-services area," says West. AmEx, whose stock has been hot—jumping from 74 in October to 103% on Apr. 15—has a market cap of \$50 billion. AIG, whose stock also has been on fire—up from 98 in late November to 133%—has

a far larger market cap: \$95 billion.

How much will AmEx go for? West believes AmEx, with revenues of \$18 billion, is worth 130 to 140 a share in a buyout. Both AIG, whose revenues exceed \$32 billion, and AmEx would benefit from a more diverse base of business, notes West, "something that AmEx needs to have, as seen from the Asian crisis' slowing effect on its American Express Bank operations."

The cross-selling opportunities are enormous, says West. AmEx would be greatly helped by AIG's global network and clout in 130 countries—and AIG by AmEx's marketing skill and franchise overseas. Last year, Citicorp acknowledged that it talked merger with AmEx, which insisted on staying independent. AmEx' Susan Miller says AmEx won't comment on rumors. Likewise, says Joe Norton at AIG.

GAYLORD SNAPS TO ATTENTION

Paper stocks appear to be waking up to the bull market, finally. Even laggard Gaylord Container (GCR), a producer of containerboard and unbleached kraft paper, has perked up, surging from 5½ in mid-January to 8. Analysts expect Gaylord, which posted a loss last year, to be in the red again this year and turn in a profit only in 1999. One thing buoying the stock is talk of consolidation.

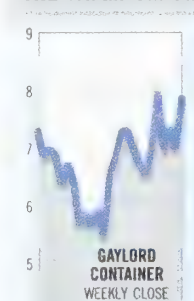
At Gaylord, a "strong and well-focused asset base makes it an attractive takeover candidate," says BT Alex. Brown analyst Mark Wilde.

Containerboard is a highly fragmented part of the industry, so consolidation may be the quick way of enhancing shareholder returns, says Wilde.

Gaylord insiders, he notes, own a fat slice of the stock. (Chairman Marvin Pomerantz has 10%). And management "appears more open now to the idea of selling the company than in the past," either a cash or stock deal. "A strategic industry player could pay 16 to 17 a share for the stock," he adds.

He thinks papermaker Weyerhae-

SET TO JOIN THE PAPER CHASE



DATA: BLOOMBERG FINANCIAL MARKETS

ser could be the likely buyer. Others he believes are interested: Union Camp, International Paper, and Jefferson Smurfit Group, a producer of corrugated cases, paper, paperboard, and newsprint. "There's limited downside risk in the stock at this price," says Wilde, who expects Gaylord to earn \$1 in 1999. Gaylord's Pomerantz says the company isn't for sale, but "it's aggressively pursuing all options to enhance shareholder value."

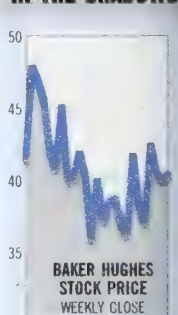
SCHLUMBERGER MAY PICK A PARTNER

Well, Schlumberger, what now? That's the question being asked by oil-patch pros ever since diversified oil-service company Halliburton announced in February that it was acquiring Dresser Industries in the largest oil-services merger ever. Whispers are that Schlumberger (SLB), the world leader in oil-and-gas drilling services, is poised to go after Baker Hughes (BHI), the world's largest maker of drill bits, whose 1997 sales totaled \$3.7 billion. Schlumberger's sales of more than \$10 billion would be dwarfed by the combined \$16.2 billion sales of the Halliburton-Dresser duo.

A New York hedge-fund investment manager insists that Schlumberger has twice approached Baker Hughes last year with an offer. So far, Baker Hughes has kept Schlumberger away, he notes. Trading at 41 a share, Baker has a market cap of \$6.7 billion. He figures that in a buyout, Baker is worth 55.

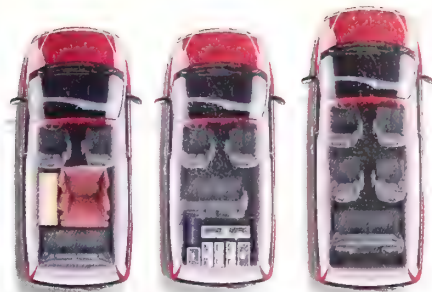
This money runner says Schlumberger, now at 78% and with a market cap of \$38 billion, has told analysts it has no immediate plans. "But being the dominant player and being relegated to No. 2 status, Schlumberger will surely have to buy someone sooner than later," says this pro. One analyst explains that Schlumberger needs to boost sales, and acquiring Baker would be a quick way to do that. Schlumberger and Baker didn't return calls.

LANGUISHING IN THE SHADOWS

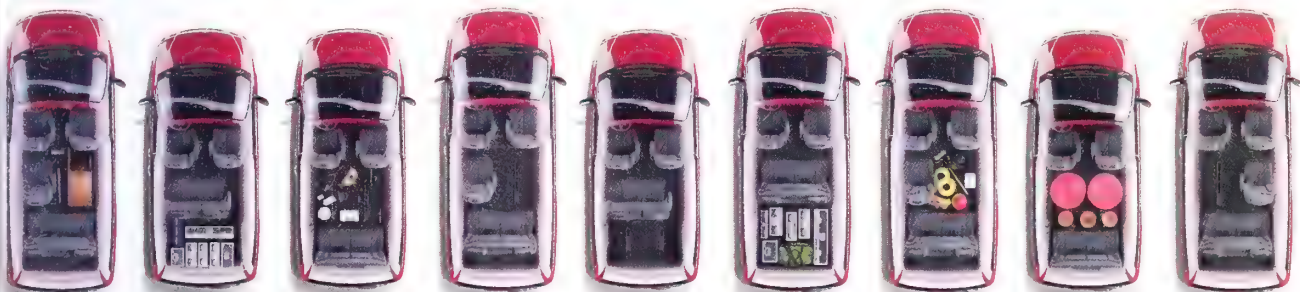


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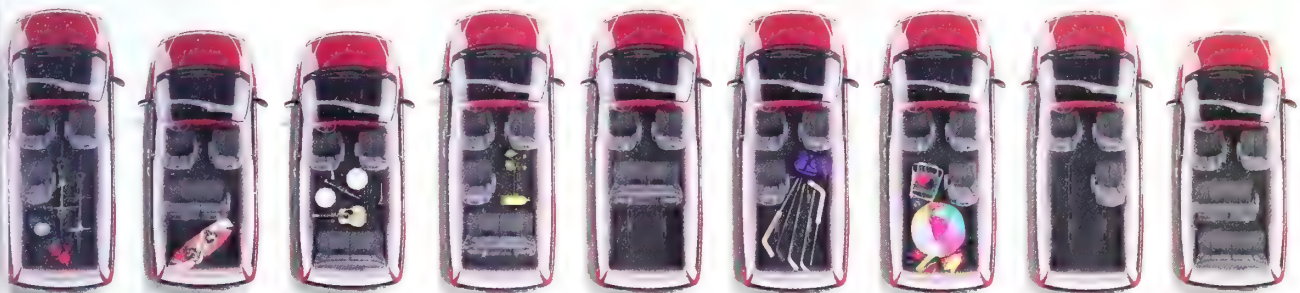
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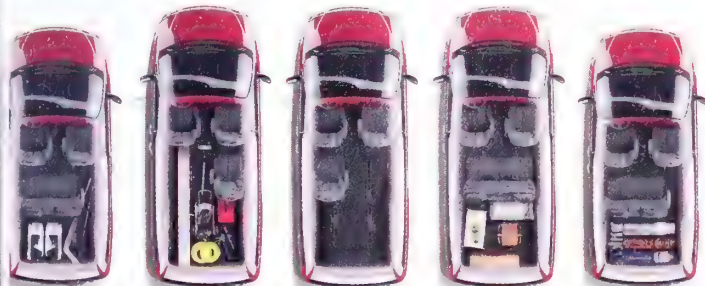
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INTELLIGENCE BRIEFINGS

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The following article appears on S&P Personal Wealth, www.personalwealth.com, the interactive investment advisory service for the individual investor:

YOU WON'T HAVE YOUR FATHER'S RETIREMENT — SO WHY SHOULD YOU HAVE HIS RETIREMENT PORTFOLIO?

Retirement investing has changed dramatically over the last 10 years. Today, with people working and living longer, the last thing on the minds of many of

Prime showed a three-year annualized rate of return of 5.50%; the Vanguard High Yield fund included here returned 13.65%, and most impressive of all, the Value Line Convertible had a return of 19.60%.

The money fund acts as the more traditional income "anchor" while the high yield and convertible provide the portfolio with higher income levels and upside total return in favorable equity market environments. This mix allows for high levels of income with greater stability. The high-income fund also allows for total return potential in favorable bond

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those who have reached the artificial "retirement" age barrier is to quit being productive. Those retiring in their early 60s may well have another 30 years on their investment horizon!

Many retirees are starting second careers and are taking a much more active part in their financial future. This dramatic change has prompted new ways of dealing with retirement and investment planning.

So, rather than offer a traditional "ultra conservative" mutual fund portfolio, we are presenting one with a different approach — an aggressive income portfolio. In this less traditional portfolio we have used just three funds: a money market, high yield and convertible bond fund. The Vanguard Money Market Reserves Prime Portfolio (VMMXX) makes up 20% of the portfolio; the Value Line Convertible Fund (VALCX) also represents 20%; and the Vanguard Fixed Income Sector Fund: High Yield Corporate (VWEHX) accounts for the remaining 60%.

These aren't just funds we picked out of a hat. These funds were selected based on their long-term records of return and risk. The Vanguard Money Market

and/or stock market environments. The convertible fund will provide lower levels of income, but much higher levels of total return.

The results of the allocation and the fund selection provide a return and risk profile that offers solid income and historical performance. On a three-year basis, the portfolio's average return would have been 13.2%, and on a five-year basis, it would have been 10.1%. The current income levels stands at an impressive 7.07%. This is more than 150 basis points higher than a money market and about 120 basis points higher than the 30-year Treasury bond. As for risk, the portfolio's annualized standard deviation, based on a five-year period, is about 4.2%. This is about 30% of the S&P 500's volatility.

The time horizon of this portfolio should be in excess of five years, and the portfolio is not intended to be traded on a regular basis. It also exposes the investor to greater downside risk than more traditional retirement portfolios. However, it is intended to allow for higher levels of total return and income. The combination of consistent performers with lower volatility should provide exposure to the markets while limiting volatility.



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SARA LEE: PLAYING WITH THE RECIPE

It's bent on making better use of its disparate brands



Pepsi is a \$23 billion brand. Reebok clothes are sold in 170 different countries. Kraft products bring in some 30% of revenue at their parent company. And all of these brands, sensibly enough, have companies named for them. Then there is the strange case of Sara Lee. The label made famous by its frozen cheesecake accounts for \$375 million in sales each year, a paltry 2% of the \$19.7 billion revenues its parent brings in. The company also owns the world's largest underwear brand, a \$4 billion packaged-meat business, and a huge food-service unit—and yet it's the cheesecake whose name is on the front door.

Now, Sara Lee Corp. is embarking on a major effort to live up to its name. Within three years, executives predict,

the Sara Lee brand will bring in \$600 million annually and will reach \$1 billion soon after that. To get there, the company has doubled the label's advertising budget, reorganized its management, and moved the brand beyond the freezer into the meat case and the bakery. Sara Lee execs admit they're playing catch-up. "The brand we've actually spent the least time focusing on is the one the company's named after," says President C. Steven McMillan. "This is a brand we have never used even remotely to its fullest potential."

LAGGING STOCK. That effort to pump up Sara Lee's namesake brand is but one example of the Chicago-based company's attempts to boost its top labels. The strategy is a critical next step in

Sara Lee's plan to transform itself from a manufacturing and sales conglomerate into a lean marketing powerhouse. In September, Chief Executive John H. Bryan announced Sara Lee would sell off factories and less important brands and use the proceeds to buy back \$1 billion of its lagging stock and invest in its core food and clothing brands.

To succeed, Bryan and his deputies must give consumers new reasons to buy Sara Lee's familiar products. Can they do it? The record is mixed. They've created successful brands in highly fragmented categories. But they'll need to demonstrate a newfound ability to compete with the giants of food and clothing.

Bryan's shift away from manufacturing to focus on brand marketing recognizes that the future belongs to companies—like Coca-Cola Co.—that own little but sell much. "It's passé for us to be as vertically integrated as we were," says Bryan, in his 23rd year as CEO. Wall Street has responded enthusiastically. In the last seven months, Sara Lee's shares have gained 50%, to around 62—as much as in the previous three years.

Outsourcing alone won't keep the stock climbing, however. Since 1992, Sara Lee profits have grown by just 6% a year. To achieve the 13% to 15% annual growth in earnings-per-share that Bryan is now predicting, he'll have to polish and expand the brands in the company's largely unexciting business mix. "They are basically mature businesses," says Arthur Cecil, who follows the company for

BEYOND CHEESECAKE

CEO Bryan wants to create a lean marketing machine by selling plant

and beefing up Sara Lee and other labels



Rowe Price Associates Inc., which owns \$3 billion of Sara Lee shares.

Until now, Bryan's preferred strategy has been to find product categories that lack a powerful brand and then build one. It worked with the Coach leather accessories line, which Sara Lee has built from sales of \$25 million in 1986 to \$500 million last year. Hanes' success is even more dramatic. The underwear brand has used new distribution channels, such as Wal-Mart Store Inc., and new products, particularly for women, to soundly thump Fruit of the Loom, the leader just a few years ago.

But in battles against larger, more creative companies, Bryan's team has

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Sara Lee's Mixed Bag

The namesake brand is one of several under the spotlight

HANES	Expansion of this underwear line made it the company's best performer. Trying to follow up with new baby clothing and loungewear.
SARA LEE	Company hopes to triple sales, turning old cheesecake label into multicategory brand that brings in \$1 billion.
BALL PARK	Top hot dog brand widened lead in 1997, partly because of increased ad budget. Will have to fend off Kraft's Oscar Meyer.
L'EGGS	Still No. 1 in a category badly damaged by casual dress trends. Is expanding into other legwear, including socks.
COACH	One of the company's most upscale brands, but brings in just 3% of sales. May be shed as part of reorganization.
DOUWE EGBERTS	Coffee line, the largest of Sara Lee's European brands. Has been hampered by currency fluctuations.

DATA: SARA LEE CORP., PRUDENTIAL SECURITIES INC., INFORMATION RESOURCES INC.

weaker record. Rivals like Kraft and Conagra have won market share by being more innovative, devising the prepackaged Lunchables meals and the megabrand Healthy Choice. And Sara Lee's Champion sportswear has failed to keep up with Nike or Reebok. "The company hasn't always done well with categories that require a lot of style," says former Sara Lee President Paul Fulton, now CEO of Bassett Furniture.

The Sara Lee food brands illustrate why—and the tough task the company has ahead. Confined to the freezer, Sara Lee for years was left to languish as its supermarket brethren branched out. Today, it sells less, advertises less, and has far fewer products than those big competitors. Pillsbury Co., for example, spent \$88 million on its flagship brand last year, more than 25 times what Sara Lee spent, according to Competitive Media Reporting. And the Kraft label appears on hundreds of products across 10 major categories.

In the '90s, Sara Lee started to change that, expanding into deli meats, opening sandwich shops in airports and on college campuses, and starting up a line of bagels. The move into deli meats was a gamble, and it met some resistance within the company. Bakery executives worried that the shift to meats

would confuse consumers. But assurances that only higher-end products would get the label helped allay fears. "You can't just slap 'Sara Lee' on a hot dog," says James R. Carlson, who oversees the company's U.S. food divisions. **PREMIUM MEATS.** At the time, a recession was driving down cold-cut prices. Sara Lee went in the other direction, calling its brand "premium" and charging \$2 more per pound. It worked; in five years, Sara Lee has captured 6% of the market. But the deli meat business is highly fragmented. Expanding some of its other brands means moving into categories where it will have to take on established leaders. Thomas', the English muffin line owned by Best Foods, and Sara Lee both entered the

fresh bagel category in the past few years. In early 1997, they were essentially tied for No. 2 with \$40 million in sales, according to Information Resources Inc. Since then, Thomas' has used its familiarity as a bread company to win shelf space and leapfrog past No. 1 Lender's, while Sara Lee's has barely grown.

How did Sara Lee bungle bagels? Weak distribution, for one. Because most Sara Lee products do not go stale quickly, the

company didn't develop an extensive fleet of trucks to deliver straight to supermarkets. "They don't have a broad-based direct store delivery program," says Donald Berman, a Best Food vice-president. It also doesn't help that Sara Lee's investments have been sporadic. Ad spending for the brand fell sharply from \$10 million in 1996 to \$3 million last year as the company emphasized its coupon program.

Now, Bryan and McMillan say such errors are behind them. By freeing up manufacturing resources, they

making a clearer commitment to Sara Lee and other brands. "We're just not cranking this up," says McMillan.

To that end, the company has placed one executive—Vice-President George A. Shivari—in charge of both the bakery and deli-meats businesses and told him to concentrate on expanding the Sara Lee brand. In the year that started on July 1, ad spending for the brand will rise to \$22 million. One big push targeting consumers who have less time to prepare food than they used to and who no longer sit down to eat as part of a large family. New products include smaller cheesecake portions that don't have to be defrosted. The company also hopes to roll out prepackaged, refrigerated meals—although early tests in Chicago haven't been very successful. Distribution of already cooked meals is always tricky, McMillan acknowledges.

Sara Lee executives will have to solve those problems and others if they hope to be considered a nimble marketing giant rather than a mishmash of shop polish and bras, sausages and T-shirts. With their namesake brand, they've got one big advantage. Just about everyone recognizes the Sara Lee label—thanks, in part, to the old "Nobody doesn't like Sara Lee" ad campaign. "Of all the baked-good products," says Richard Gerstman, president of Interbrand Gerstman+Meyers, a New York consulting firm, "Sara Lee probably has the best name." Of course, if their efforts fail, there's another option: Bryan can rename the company Hanes Corp.

By David Leonhardt in Chicago

THAWING OUT

The company has expanded beyond the freezer and into fresh baked goods



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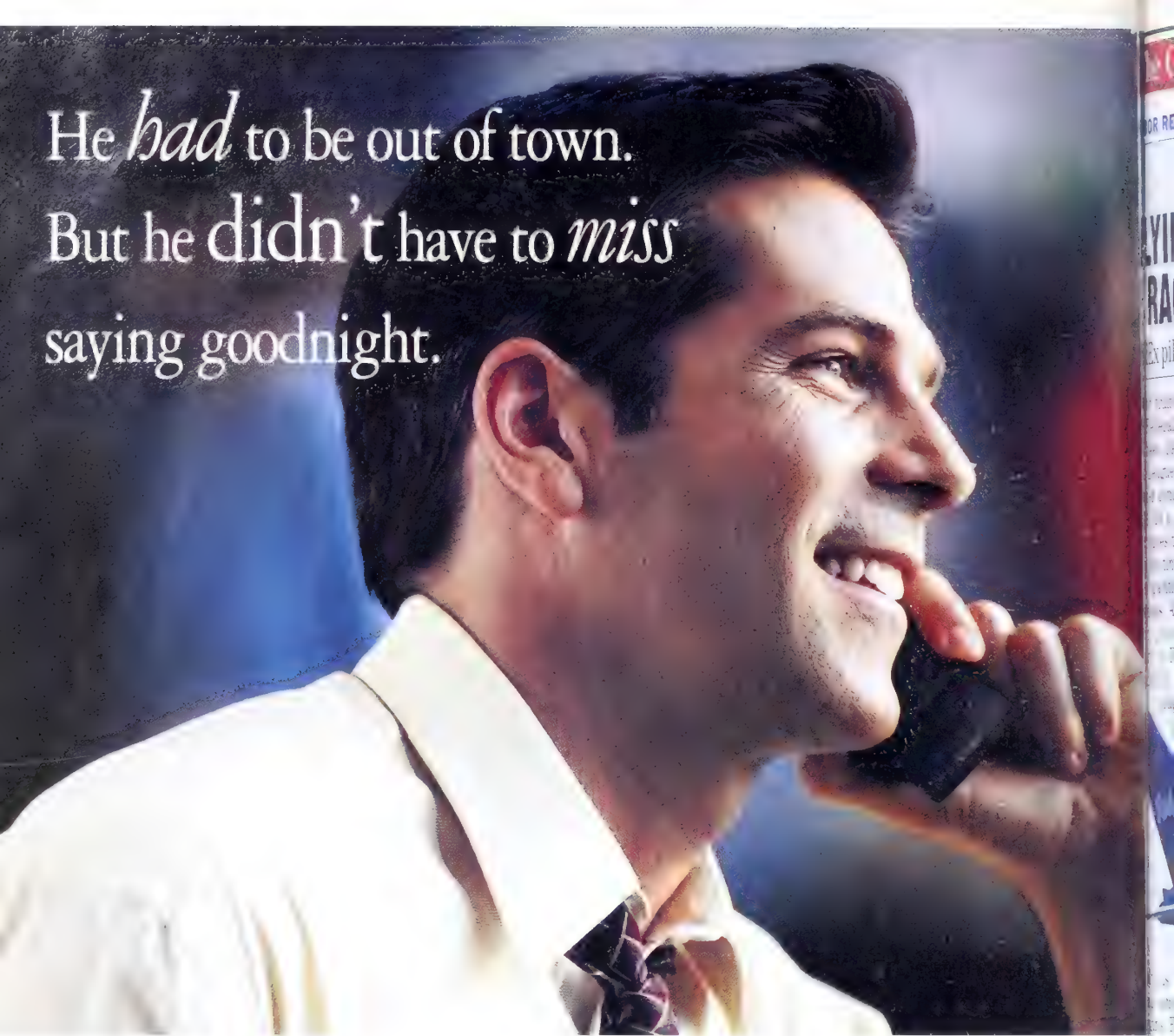
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LYING INTO RAGE?

Ex pilots are talking tough after rejecting a new contract

r trained pilots, landing a job at Federal Express Corp. has long been like getting accepted to the League. The highest-paying of all other companies, FedEx starts pilots \$310 a month; veterans earn up to times that. Other benefits, such as for time spent away from home, traditionally been among the most lous. And in return for great treatment, pilots have showed remarkable y to FedEx and its brash founder, erick W. Smith. Many have bragged that their blood ran purple, the color of the express-mail giant's logo.

Now, however, that

Still, the issue is unlikely to go away. Pilots complain that FedEx is offering only a 4% increase for the first year of the pact and an 11.4% raise over its four-year term, even though pay has improved little since 1990. Their anger has been fueled by the 23% raise and more flexible scheduling their counterparts at United Parcel Service Inc. won in March.

But pay isn't the only issue steaming FedEx pilots. Under the proposed contract, the flexible work schedules that had been a FedEx hallmark could become as rare as ex-

tra legroom in coach class. The pilots are particularly unhappy with proposed changes in work rules that would trim the amount of pay they get for downtime when away. The proposal also would allow FedEx to subcontract work to nonunion pilots flying leased planes.

Add it all up, and FedEx has one unhappy group of flyboys—and 'girls—on its hands. Some pilots are even openly discussing possible work slowdowns. "The only tool available to us is to impact reliability and service," says 25-year veteran pilot Richard D. MacGibbons. That could seriously threaten on-time deliveries at the company, which relies on airborne freight for most of the 3 million packages a day it delivers. "The company doesn't function without the pilots," says analyst Paul R. Schlesinger of Donaldson, Lufkin & Jenrette Inc.

Maybe not, but FedEx may have little choice but to clip the pilots' costly wings. Stiffer competition, rising costs, and a move into lower-margin business-

es have trimmed its operating margins from 11.5% in 1987 to 6.1% in 1997.

Moreover, FedEx now has the highest cost structure of its major rivals, Schlesinger says. Even after the big raise UPS pilots gained, veteran FedEx captains still make more—\$13,689 a month, vs. \$13,195 a month at UPS, according to pay consultant Air Inc. "FedEx is realizing that it can't afford to pay high wages and fly expensive planes when its competitors are flying older planes and paying pilots less," says David F. Hoppin, a principal at air-cargo consultant MergeGlobal.

UNION BID. For now, however, talks are on hold. FedEx says it can do little until the union sorts itself out. Union head Michael Akin has surveyed members on why they vetoed the deal and asked to restart talks. "We want to make sure [the pilots] get exactly what they feel they deserve," says Akin. But many pi-

lots say they remain unhappy with the union and fed up with Smith's perceived lack of action. "The company doesn't want to sit down and look at what's right," says veteran Don Wilson.

Of course, FedEx' silence may be little more than a bargaining tactic. "All we're seeing here is a tough negotiation process," says Keith A. Patriquin of Loomis, Sayles & Co., which owns 99,000 FedEx shares. Still, FedEx is clearly paying a price for its toughened stance. Over the past two years, membership in the union has grown from 45% of pilots to 82% today.

Dissatisfaction may be spreading. Though FedEx says workers can receive annual pay raises as high as 7%, some ground workers get much less. Efforts by the Teamsters to capitalize on the pilots' unhappiness in its bid to unionize FedEx' 100,000 ground workers appear to be bearing some fruit. "Watching what the pilots are going through is making me think more about the Teamsters," says a nine-year FedEx courier in Tacoma, Wash. Still, the Teamsters effort is in the early stages.

So far, customers have not been affected. Having suffered through last year's UPS strike, they can only hope that remains the case.

By Nicole Harris in Atlanta

FED UP:

Why FedEx pilots rejected their contract

- 11.4% pay raise over the next four years—far less than at rival UPS
- Less control over scheduling
- Longer hours, often for no more pay

y is wearing thin. In the face of g competition and sharply reduced ins, FedEx is trying to rein in its cost pilots. But in March, angry en rejected a proposed contract ed by their own union leadership, umblings of a possible work stop- are on the rise. Worse, the prob- with unhappy pilots could spread her workers. For a company whose ho *esprit de corps* has long been al to its success—and its high ser- levels—that could mean trouble. re was a trust relationship that has 'iorated," says pilot Kevin Scheit- a, a nine-year veteran and one of pilots who voted against the new act. "A lot more guys are not will- o give 100%."

DOFF. FedEx officials downplay the ulties. They refuse to discuss the fies of the pilots' situation, saying that the next move is the union's. h—who has long made a point of ring good relations with his work- —declined requests for an inter-. A company spokesman disputes workers are unhappy, citing annual yays filled out by 97% of employees.



EDITED BY AMY DUNKIN

SUDDENLY, BOXY IS BEAUTIFUL

Did Alfred P. Sloan Jr. ever dream that someday carmakers would aspire to build a truck, not just a car, "for every purse and purpose"? Surely, even the master marketer who ran General Motors from 1923 to 1956 didn't foresee the day when Cadillac would plan a top-of-the-line sport-utility vehicle while BMW prepared a "sports activity vehicle" and Lincoln a deluxe, wood-paneled pickup truck.

And that's just the beginning. As America's love affair with all things big and boxy continues, auto makers are spinning off a dizzying variety of new luxury trucks and sport-utility vehicles on steroids (table). In SUVs alone, the industry will increase its offerings from 32 models just two years ago to 69 by 2005, according to Santa Ana (Calif.) consultants AutoPacific.

HYBRIDS. Even the definition of trucks—a category that includes vans, minivans, SUVs, and pickups—is expanding to encompass trucklike cars: a burgeoning class of all-wheel-drive station wagons and a new breed of car-truck hybrid such as Toyota's RAV4, Honda's CR-V, and Lexus' RX 300. Says Chrysler Chairman Robert Eaton: "All the trucks and sport-utilities are going like dynamite."

For good reason. Consumers love the improved view that comes with riding high and the security of sure-footed four-wheel-drive in bad weather. In exchange, they're

willing to forgive dismal gas mileage, high step-in heights, a sometimes jolting ride, and less-than-precise handling. Even recent safety studies showing SUVs may pose an increased crash threat to small cars seem to be convincing drivers that they and their families are safest inside a well-armored truck.

More than anything else, what U.S. drivers crave—and trucks give them—is lots of seating and cargo space. Sharon Koorbusch, a Leesburg (Va.) pharmaceutical sales rep, is on her third minivan. She says her four-door Chevrolet Venture is perfect for carting her two children and two Labradors, plus kiddie seats, stroller, diapers, food, and play gear. And it's great for hauling drywall or furniture. "I could never go back to a car now," she says.

Other consumers seem more interested in how many amenities they can cram into their minivans. Chrysler has been astounded by the popularity of its Town & Country, whose sticker tops \$35,000 fully loaded. Chrysler sells

about 80,000 a year now, up from just 25,000 in 1993. Conversion companies are busily installing TVs and VCRs in vans and big SUVs and starting to add conference tables and computer hookups to the Internet.

Roberta Clarke, a Boston University marketing professor, has a theory about why. In the late 1980s, people liked holing up at home with their loved ones and plenty of creature comforts. Now, thanks to cheap gas and busy schedules that keep them and their kids on the road, baby boomers jam all that stuff, including CD players, cup holders, and fax machines, into their autos. "They're cooing in their cars now," Clarke says.

The fascination with trucks may also reflect the baby boomers' last-ditch effort to cling to the symbols of their fleeting youth. Clarke says that she sees signs of the youth cult in the current obsession with SUVs. "Part of it is boomers beating their chests, saying, 'I'm

not old yet. With a four-wheel-drive, I can still drive into the woods, I can still hike. I'm rough and tough," she says.

SIREN'S CALL. In addition, trucks have become a symbol of freedom. The more crowded, rushed, and complicated life in the late '90s becomes, the greater the lure of the open road—better yet, the trackless wilderness. True, only 15% of SUVs, at most, ever go off road. Yet driving a rugged sport-utility is seen as a way

to prove to the world you aren't just another frazzled suburbanite—even if you are. "They clearly are symbols that you're a person who's independent and self-reliant," says Michael Marsden, dean of the College of Arts & Sciences at Northern Michigan University, who teaches about the automobile



CARGO SPACE AND LUXURY, TOO

MODEL	BASE PRICE	COMMENTS
AUDI A4 AVANT QUATTRO	\$31,540	Newest all-wheel-drive wagon
GMC YUKON DENALI	\$43,495	GM's first large luxury SUV
LEXUS RX 300	\$32,045	The first luxury hybrid car-SUV
LEXUS LX 470	\$55,445	Deluxe off-roader
MERCEDES-BENZ ML320	\$34,545	The hottest compact SUV

*Suggested list price plus destination charge

DATA: COMPANY REPORTS



will have a V8 version of the ML320 out later this year, selling for under \$45,000. The new \$55,445 Lexus LX 470 now arriving in showrooms comes equipped with more standard features, including reclining rear seats and a smog sensor, than even Lexus' flagship LS 400 sedan. GMC is adding the Yukon Denali, a deluxe version of its big Tahoe SUV. Even that will be upstaged this fall, when Cadillac introduces its fancier version, the Escalade.

In their quest to make SUVs more like cars, the latest trend is the car-truck hybrid. These crossover vehicles look like sport-utes but handle with the finesse of cars—because they're based on a car chassis. Following the success of the small, sporty RAV4 and CR-V, Lexus on Mar. 23 launched its RX 300, a luxury SUV based on the ES 300 sedan.

TOO CLUNKY. As SUVs become more carlike, some cars are bulking up to compete more with trucks. The once-scorned station wagon is reinventing itself. Even some of the outdoory types who were hardcore truck owners are now going for husky, all-wheel-drive wagons. Take Dewey Moser, 55, a New York stockbroker who owned an Isuzu Trooper for hunting and hauling his boat to the shore. But he says he didn't like the truck's clunkiness: "At this stage of my life, do I really need to be banged around by a truck?" So he swapped his

Trooper for an Audi A6 Quattro wagon. "The cargo capacity is tremendous, and the ride is just superb," Moser says, enthusing about his wagon's easy handling of tight highway curves and bumpy dirt roads.

Are you ready to get behind the wheel of something big and boxy? Your menu of choices has never been better, as the days of one-size-fits-all trucks fade as surely as did the Model T. *Kathleen Kerwin*

"Part of it is boomers beating their chests, saying, 'I'm not old yet.... I can still drive into the woods, I can still hike'"

Poseur Sport Utility Page Web site (poseur.4x4.org) spoofs the trend with a pitch for the fictional Kenworth Dominator sport-ute: a \$200,000, eight-ton, 20-seat monster based on a semi with 10-wheel drive that can tow your camper and yacht.

Parodies aside, the 31-flavors approach to trucks could just be boomers' way of putting their own twist on the big, cushy land yachts their elders drove. They yearn for the same creature comforts as generations past. Their vehicle of choice has a soft suspension, plush carpeting, leather seats, and a blinding amount of chrome on its grille, but it's a Toyota Land

Cruiser or a Lincoln Navigator—not Grandpa's Cadillac Fleetwood.

Certainly, trucks have rumbled into the high-rent district in ways no one could have predicted a decade ago. Sales of luxury SUVs surged by 291% last year. One of the hottest vehicles in the U.S. now is the Mercedes ML320, a new compact V6 SUV starting at \$34,545. Mercedes

American culture feeds these fantasies with images of SUVs perched on remote mountaintops. The all-American conviction that bigger is better is transforming the truck experience. Detroit has super-sized the SUV. Ford's smash-hit Expedition and Lincoln Navigator jumbo SUVs are joining the Chevy Suburban, mammoth sport-ute once revered mainly by those towing boats and trailers, at shopping malls and country estates. Not satisfied with that, No. 2 auto maker has plans for an even bigger SUV to dwarf the competition. In recreational vehicles, labeled as wheels for non-driving retirees, are hanging on with younger boomers, according to a recent study by the University of Michigan. These extremes have inspired satirists. The Ultimate

NOT YOUR MOTHER'S STATION WAGON

I was cruising down the expressway, coffee cup in one hand, steering wheel in the

other, when flashing red lights appeared in my rear-view. Usually, I lumber to work in a '94 Chevy Blazer sport-utility vehicle. But today, I'm hurtling along at 85 mph in a sleek, green Audi A4 Avant station wagon. Its handling is so smooth I didn't know I was speeding. When I say that to the annoyed cop, he tells me to act my age and lets me go without a ticket.

Who knows whether the officer was just in a good

growing weary of SUVs. The wagons offer the SUVs' generous cargo room and secure handling in adverse conditions. But they omit the rugged, jouncy ride. Since the wagons are lower to the ground, children don't need a step stool or a boost to climb in.

Of the three wagons I drove, Audi's wins in panache. The A4 Avant keeps the sculptured look of the popular A4 sedan.

Its taut ride and handling lose no curve-hugging powers in the translation to station wagon. Much of that is thanks to Audi's outstanding Quattro all-wheel-drive system, which electronically sends extra torque to



**AUTOS
WAGONS**



AUDI A4 AVANT

Base Price:

\$31,540

The Avant wins in panache, but its back seat is too cramped even for children

mood that morning, or simply wanted a close-up look at my wagon. It wouldn't have surprised me if it was the latter. The all-wheel-drive A4 Avant, along with the Volvo V70 and Subaru Outback, are ushering in a new age for the station wagon. Unlike bulky old Country Squires, these new wagons are drivers' cars that borrow features from SUVs, such as all-wheel-

drive transmissions. In fact, the new wagons are an ideal respite for those

SUBARU OUTBACK LIMITED

Base Price:

\$25,090

Plenty of cargo room and a solid all-wheel-drive system



room to stretch out in the car's plush leather seats, front and rear. As always, Volvo's safety features are first-rate, with standard front and side air bags and lap-and-shoulder belts for all three rear pas-

sengers. (The Audi also comes with these features. But the V70 XC is no lumbering box on wheels. Its 190-horsepower, five-cylinder engine has a turbocharger that gave it the best acceleration among the wagons I drove. While it doesn't handle with the A4's precision, the V70's ride is solid and secure thanks to an all-wheel-drive transmission mated to a traction-control system. The V70 XC is priced in the middle of the luxury pack, starting at \$37,960—less than BMW and Mercedes wagons but more than Audi's. A V70 all-wheel-drive wagon, without the off-road upgrade, starts at \$34,995.

ROOMY. The Subaru Outback blazed the trail for all-wheel-drive wagons when it took the market by storm two years ago. It still provides the best value, with sticker prices starting at \$22,990 and topping out at \$27,090. The Outback's four-cylinder, 160-horsepower engine is no match for those in the Audi or Volvo. Its ride doesn't come up to that of the Europeans, either. But for functionality, the Outback delivers with a roomy cargo area and a solid all-wheel-drive system.

VOLVO V70 AWD

Base Price:

\$34,995

A steady and secure ride, plus the expected first-rate safety features



These sleek and sporty wagons may one day be as ubiquitous as SUVs. For now, watch it on the road. With their superior comfort and handling, they're a pleasure to drive—almost too much of one, as I found out. *Keith Naughton*

YOU SHOULD KNOW WHAT INVESCO KNOWS.TM

In the financial world, knowledge is king. And the trick is knowing where to get it and how to use it. At INVESCO, we've been managing money in every kind of market in every kind of economy for 65 years. Our 38 no-load funds, including 11 sector funds, provide a wide range of international, growth, value, income, total return, tax-free and money market options. You can experience our

wealth of knowledge and global perspective firsthand through your financial advisor, your retirement plan at work, or by contacting us direct at www.invesco.com or 1-800-2-INVESCO. We'll send you a prospectus on any of our funds with information regarding management fees, risks and expenses. Please read it carefully before you invest or send any money. Then you'll know.



INVESCO

A SPORT-UTE MINUS THE MACHISMO

Face it. For most owners, sport-utility vehicles are more a lifestyle statement than an answer to adverse road conditions. Sure, some people need a sport-ute to tow an Airstream or navigate rutted trails on the way to a campsite. But the rest of us are just looking for cargo space to stow Little League gear or the extra confidence of four-wheel drive in winter.

Now, Lexus has an SUV for the rest of us: the RX 300. Unlike traditional SUVs such as the Jeep Grand Cherokee, Ford Explorer, or Land Rover Discovery, the RX 300 isn't up to such off-road tasks as climbing mountains. But Lexus didn't build a traditional SUV. It designed a luxury car that looks like an SUV.

Engineers at

Lexus parent Toyota stripped away attributes SUV drivers don't like: the truck-like ride and handling, the steep climb to the seat, the abysmal fuel economy. But they kept the features most buyers want in an SUV, such as the high ride height, interior roominess, and ample cargo capacity. Then they built the new vehicle on a car platform instead of that of a pickup. They threw in all the luxury features that befit a Lexus and priced it starting at \$32,045, including destination charges, for a two-wheel drive version, or \$33,445 for the all-wheel drive model. That's \$1,100 less than its most direct rival, the Mercedes ML320.

LEXUS RX 300

Base Price:

\$32,045

Not rugged enough to climb mountains, but loaded with luxury

From the outside, the Lexus is more stylish than most SUVs, with jewel-like, multi-lens headlights and taillights that would look at home on a family sedan. It's slightly

longer and wider than a Grand Cherokee, and it sits 7.7 inches off the ground, offering more clearance than an Explorer. But it's on the road where the real differences show. The ultrasmooth V6 engine, a new version of the power plant inside the ES 300 sedan, delivers 220 horsepower, more than most SUVs. Its acceleration is among the best in its class, going from 0 to 60 mph in less than nine seconds. The engine meets the stringent California low-emission standards and gets decent fuel mileage of 19 mpg in city driving and 22 mpg on the highway.

Inside the cabin, the feel is more minivan than SUV. Climbing in is easier, with no need for running boards or grab handles. But, like a minivan, the RX 300 has high seats and a steeply raked windshield. And the center console doesn't extend into the cabin, dividing the driver and passenger space. Instead, there's a flat floor with a plastic tray to keep a purse or personal planner from sliding around. Between the seats, a storage unit has an ashtray, two roomy drawers, and four cupholders.

The instrument panel has the

trademark Lexus illuminated gauges. Audio and air-conditioning controls are in the center console, along with the shifter, in a U-shaped pod surrounded by walnut. The pod also holds the one thing about the controls I didn't like: a 5-inch blue-and-white LCD display that shows temperature, time, audio choice, and continuous trip information, such as time elapsed and average fuel economy. It looks like a big TV tube in the middle of an otherwise uncluttered dash.



**AUTOS
SPORT-UTES**

Every luxury amenity is available. An \$1,800 premium package adds leather seats; heated self-dimming mirrors; bright lights behind you; programmable garage-door opener, and an air filtration system. A tilt-and-slide moonroof is \$1,000. A six-CD changer in the glovebox costs \$1,000. Side air bags are standard. **SNIPING.** Rear legroom is especially generous, and the rear seats can move forward and back nearly five inches, allowing a trade-off between legroom and cargo space. In the forward position, they also recline, or the seat backs can be folded down for a level cargo surface that opens up 75 cubic feet of storage.

Still, rivals will snipe that it's not a "real" SUV, that it can't climb mountains or do other Marlboro Country stuff. I'm betting Lexus will sell every one of the 20,000 it makes this year because more of us are looking for a family car than a he-man truck.

Larry Armstrong



KINDER, GENTLER Better gas mileage and acceleration, a smoother ride, and it's easier to climb into

CONCERT ALL IN A TRUCK

ore the sport-ute
m of the 1990s,
t-truck owners
e more

ested in high
d clearance than
fidelity. Thus,
"audio sys-
' usually
sted only

ie-speaker AM radios.
just wanted a radio for
farm report," says
rd Stroud, supervisor of
acoustics for the Delco
ronics Div. of General
rs.

lay, as drivers ditch the
y car in droves for
-utility vehicles, mini-
and four-door pickups,
stereo standards are
ng. Audio engineers are
ming up to 10 speakers
trucks' cavernous con-
and making them sonic
pieces.

VING. An AM/FM stereo
comes as standard equip-
on most trucks. But

buyers are opting for
ple-CD players and dual-
stereos, which allow the
to listen to Puff Daddy
eardphones in the back
mom and dad groove
ric Clapton up front.
e plenty of people are
ig to spend more than
0 to get a custom sys-
from an independent
o shop, many buyers are
ly taking the premium
o package that is in-
d at the factory.

own the road, trucks will
re even more high-tech
o extras, such as digital
und-sound stereos like
e found in home enter-
ent systems. "These ves-
es are ripe for that kind
nfiguration, because you
speakers all around

you," says Henry Blind,
Ford's senior technical spe-
cialist for audio acoustics. The
sheer size of most trucks
makes them a hospitable
habitat for big sound. There
are more spaces for speakers
than in the family sedan. And
the music has more room to
move around, heightening the
separation of sound and cre-
ating an audio experience
usually found in your living
room.

Indeed, buyers are now
demanding more creature
comforts as truck prices
reach for the sky.

"There are a lot
more affluent truck
buyers, and they're
looking for the
same kinds of
amenities they
found in luxury
cars, if not more,"
says Michael Mal-
oney, director of
multimedia systems for
Visteon, Ford's parts
unit. That's why 73% of
buyers of the \$45,000 Lincoln
Navigator order the \$950
Mach audio system with sev-
en speakers and a six-disk CD
changer housed in the center
console.

But trucks also provide
plenty of problems for audio
engineers. For starters,
"you're constantly being chal-
lenged by road noise," says
Maloney. Feedback from
brawny engines also intrudes

MORE SPACE The sheer size of trucks makes them a hospitable environment for big sound

in the cabin. To drown out
the noise, engineers boost
amplification, jack up the size
of speakers, and even hang
them from the ceiling. For
example, the 10

speakers on the
Jeep's Infinity Gold
system—a \$280 to
\$940 upgrade—in-
cludes four tucked
into the roof. Two of
the eight speakers
also line the roof
in the Chevrolet
Suburban's \$200

premium audio pack-
age. "Speakers play
loud and clear when they are
close to your head," says
Stroud.

Another problem: Trucks'
wide-open spaces are not con-
ducive to the thundering bass
preferred by many audio-
philes. With car stereos, the
trunk provides a natural res-
onance chamber. But trucks
don't have trunks, so engi-
neers have to be creative. GM
and Chrysler pump up the
bass by drawing it from

speakers placed in the large,
deep doors found on trucks.
Ford generates a booming
sound from a beefy 8-inch
subwoofer encased in thick
plastic and tucked into the
rear of the Expedition.

BAD CHOICES. Where to lo-
cate the CD player poses still
another dilemma. Audio en-
gineers would like to plug
multiple-CD changers direct-
ly into the dash, instead of
tucking them away in the
center armrest, or, worse yet,
in the back.

But until minidisks or
higher-capacity CDs catch on,
bulky multidisk players are
not likely to claim prime real
estate on the dash—especial-
ly if they take space away
from those coveted cuphold-
ers. "It's a struggle, because
what we're trying to do in
truck audio is still new," says
Chrysler's Jack Mills, man-
ager of Jeep electrical engi-
neering. "But our star is
rising." Indeed, the farm re-
port has never sounded so
good.

Keith Naughton



**AUTOS
AUDIO**

REPORT ON THE 1997 CONFERENCE

The Business Future of the Americas

Presented by

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"There is no doubt..." Or is there?

"There is no doubt where this hemisphere is headed: It is moving toward a full, open Free Trade Area of the Americas. The only question is whether U.S. political leaders will recognize the reality." **Charles Preble**, president of the Association of American Chambers of Commerce in Latin America, set the tone for this year's *AACCLA/Business Week Conference on THE BUSINESS FUTURE OF THE AMERICAS*. The U.S. is out of step with the rest of the Americas. 'Awake ye American slumberers' was a recurring theme at the conference. But is Congress listening?



ARE YOU PAYING ATTENTION TO THE TRADE AGREEMENTS?

"NAFTA gave GM an opportunity to rationalize our manufacturing. For the first time it made sense to build high volume, high quality products in Mexico, both to sell there and to ship out. Our Mexican engineers developed a right-hand drive Suburban for Australia and South Africa. We are shipping from Mexico to Central

America, Egypt, the Middle East, Ecuador, Peru, and Chile. That new trade agreement between Mexico and Chile has allowed us to greatly increase our transactions there. Mexico has trade agreements with the U.S., Canada, Chile, Bolivia, Costa Rica, Colombia, and Venezuela. The Mexican government is working on many more, including the European Union and Israel. We watch the agreements very closely because they allow us to effectively use our manufacturing footprint in Mexico. The companies that stay on top of these trade agreements and react to them quickly are the companies that will be successful."

Gary Cowger,
president,
General Motors of Mexico

MORE TRADE AGREEMENTS MORE GROWTH

"Continental Airlines' Latin American business was up 40% in 1997. It will be up another 40% in 1998. We are bullish on Latin America because we see favorable market potential. There has been a tremendous economic transformation here already with governments lowering barriers, encouraging private investment, and undertaking a democratic transition. As the region works through multilateral trade agreements the market potential is even more favorable."

Ralph Schulz,
vice-president, Continental Airlines



BusinessWeek

THE BUSINESS FUTURE OF THE AMERICAS



NEED MONEY?

"Traditionally the Inter-American Development Bank has been a public sector institution,

ing principally with governments. Now we're working directly with the private sector funding infrastructural projects across the continent. We will finance up to 25% of projects in highways, roads, ports, water, and other similar areas and social areas. These are very promising areas and I am personally very enthusiastic about working with the private sector. There is growing demand. Companies are welcome to approach us directly. While the governments involved still have approval authority, we see encouragement from government to go ahead and attract private investors."

Enrique V. Iglesias,

President,

Inter-American Development Bank (IDB)



THE INTERNET IN LATIN AMERICA

"The Internet phenomena is so prominent in the U.S. that it will occur in

Latin America with just a few months' delay. That is the time lag: a few months, not more. There is a great willingness among companies in Latin America to begin applying the tools of the Internet to their business activities. Many senior executives here actually surf the Internet themselves. Many have Internet-enabled partners in the U.S. driving them to act. Smaller operations here have the most to gain: Companies that do not have the resources to set up traditional distribution channels see the Internet as their way into the global marketplace."

Dieter Linz,

IBM enablement manager,

Lotus Development Corporation

TIME TO UPDATE YOUR LATIN AMERICA STEREOTYPES

"Most Latin American countries are now achieving single-digit inflation. This is the single most important economic success story of the 1990s: Latin America has growth with financial stability. The quality of macroeconomic management has improved dramatically. The elements that led to the Mexican debt crisis are not found in any country in Latin America today. Not one."

"Fiscal affairs have been brought under control. The 1980s average Latin American country fiscal deficit of 5%-to-6% of the GDP has been driven down to around 2%. I do not see any possibility of a repetition of the 1980 crisis, not even remotely."

"There has been an important redefinition of the frontier between public action and private action. States that were involved in production are becoming states involved exclusively in regulation."

"There are much lower taxes on international trade, and there has been a deregulation of financial and labor markets."

Gert Rosenthal, Executive Secretary, United Nations Economic Commission for Latin America and the Caribbean



TAKE LATIN AMERICA

The Asian tigers are now pussycats. Latin America, Central America, the Caribbean, and South America are the new tigers of industry. We can be very proud, all of us here in this continent, of what we have done and of what is going to happen in Latin America."

Cardo Cabrera, vice-president, Latin America, Bellcore

There have been more telecommunications privatization initiatives in Latin America than in the rest of the world combined: 41 in 1997 alone. There is a convergence of political, social, economic, and technological forces moving our hemisphere to levels of growth that were unthinkable a decade ago. The barriers to entry are falling and capital, both financial and intellectual, is flowing at an enormous rate."

Argemiro Araz Guereña, managing director, Central America, AT&T

South America has been a leader in liberalization and privatization. We see a move from government-owned corporations to privatized companies, and the introduction of competition. More players and business people have every opportunity to convey to government what is needed to be successful. So it is a very logical, very practical set of considerations that lead us to place an emphasis on South America."

Francis Urbany, executive director, international, BellSouth

Latin America is our major area of emphasis because the agents of change are moving here. The antiquated approach is totally gone. The continent has capitalist markets. It is privatizing state enterprises, and it has market forces driving change. This is a winning formula."

Edward Doody, vice-president, senior manager for international banking, Mellon Bank

THE GUATEMALAN SUCCESS



Hon. Alvaro Arzu,
President of Guatemala

"Ambassador Planty quoted a prominent economist as saying 'the momentum for economic reform in Guatemala is more overwhelming than in any other country in this region.' That is indeed the case. And our process of change is of direct and immediate interest to the Guatemalan, U.S., and Latin American business communities. We are drawing up and implementing a completely new blueprint for Guatemala: A dramatic transformation that is broadening access to wealth and opening our vast, untapped productive capacity. We are achieving this simply by putting in place the right conditions for business and investment, not only for the present but for the future. And our results can already be seen: rapidly increasing foreign investment, rapid and sustainable economic growth."

"President Arzu has Guatemala well-embarked on a process of reform characterized by enhanced opportunities for business and productive investment. The U.S. strongly supports the reforms. The progress of the past 12 months has been impressive, and it has occurred because of President Arzu's conscious and courageous decisions. His initiatives are a comprehensive program for the future and they have the strong support of the U.S. government."



H.E. Donald J. Planty,
U.S. Ambassador to Guatemala

WHY ARE SO MANY LATIN AMERICAN COUNTRIES ENTERING INTO BILATERAL TRADE AGREEMENTS WITHOUT THE U.S.?

Guatemala imports roughly \$420 million worth of goods from neighboring Mexico, while Mexico buys only about \$80 million worth of Guatemalan products. Despite this level of imbalance,

Guatemala is actively pursuing a free trade agreement with Mexico. Why? Guatemala's reasoning illuminates the new free trade perspective of Latin America, and also holds lessons for U.S. thinking on the free trade issue.

"The worst thing for Guatemala would be to maintain the status quo. Guatemala is a very open economy while the Mexican economy is very closed. Besides freer access, a trade agreement will include a legal framework to govern the Guatemalan trade relationship with Mexico: norms, rules, and regulations that are legally binding, with full mechanisms for the solution of any controversies that may arise. That is much better than trade based on what kind of day the governor of Chiapas or the mayor of Tapachula happens to be having. Clear conditions for each country's access to the other's market. That is our goal."

Hon. Juan Mauricio Wurmser,
Minister of Economy,
Guatemala

FREE TRADE: WHY WE GOT TO HAVE IT

"One-third of the remarkable economic growth the U.S. has enjoyed in the past four and half years has come from exports. With more than 12 million jobs depending on export sales, the continuing increase of U.S. exports is absolutely essential to the continuing health of the American economy. But counter to-country bilateral trade agreements that exclude the U.S. are making it more difficult for U.S. companies to maintain the growth, particularly here in Latin America. For example, Canada now has a trade agreement with Chile eliminating an 11% across-the-board tariff. That is an 11% advantage for Canadian firms every time an American firm tries to compete with them in Chile. The European Union is working on a bilateral trade agreement, too, and on one to cover Argentina, Brazil, Paraguay, and Uruguay. All these leave the U.S. on the outside looking in at the very markets that will drive 21st century economic growth."

Hon. Marjorie Searing,
Director General of the U.S.
and Foreign Commercial Service;
Acting U.S. Assistant Secretary
of Commerce



THE BUSINESS FUTURE OF THE AMERICAS



ACTING GLOBAL? BETTER HAVE LOCAL HELP

"There is an enormous focus on globalization here. When a company comes into Latin America from abroad it usually sets up in several countries at once and must immediately establish communication among its Latin American units

as with its headquarters. This 'instant multinational' effect creates that a certain uniformity be present in the technology each national company selects. Companies cannot achieve this in Latin America: They need to work with local integrators and coordinate the linking process among the pieces. More elsewhere, local support is a critical component of the soft-selection and implementation process in Latin America."

Roberto Gonzalez, regional vice-president, Baan Company

WAS CLOSED... IS NOW OPEN

"The opening to private investment is a tangible process in today's Venezuela. There are now 60 companies from 14 different countries performing various activities in our upstream petroleum sector. And there are opportunities in petrochemicals, gas distribution, outsourced services, and refinery stream industrialization. All this is a direct result of our economic opening."

Manuel Pulido, director, Petroleos de Venezuela

PROFITING FROM THE PROGRESS IN LATIN AMERICA

"Latin America is of growing strategic importance to a growing list of industries," says **Dennis Whitelaw**, president of the American Chamber of Commerce of Guatemala. "It is a natural expansion market for a company such as Marriott." THE BUSINESS FUTURE OF THE AMERICAS conference was held at the newly remodeled Hotel El Dorado in Guatemala City, now a convention center named the Guatemala City Marriott where Whitelaw is the general manager. "Guatemala's government is on the right track with business reforms and dramatic improvements in the national infrastructure. Add in the NAFTA extension, amplification of the Caribbean Basin Initiative, 'fastrack' authority to speed U.S. trade negotiations and a Free Trade Area of the Americas, and you will see more and more American companies turning into genuine multinationals — and heading for this region."



Dennis Whitelaw, president, American Chamber of Commerce of Guatemala

LATIN AMERICA IS ON A FAST TRACK TO ECONOMIC INTEGRATION — WITH OR WITHOUT THE U.S.

Economic integration is going forward across Latin America. Mercosur has been quite aggressive in negotiating with Chile and is currently negotiating with the Andean Pact. There are many examples of bilateral agreements, and a growing Latin American consensus on this. The worst-case scenario of no fast-track and no negotiations will still include economic integration and continuing liberalization among the Latin American countries. Have no doubt about that."

Dr. José Manuel Salazar, Minister of Foreign Trade, Costa Rica

The question now is who is going to take the leadership role? It is clear that without fast-track authority the U.S. cannot carry out this process. We are not sure if Mercosur can assume the leadership, because right now it is deep in its own process of market enlargement. But Mercosur is nonetheless moving fast to consolidate a SAFTA, a South American Free Trade Agreement. If the U.S. does not have fast-track authority we will probably see SAFTA consolidation in the near future."

Dr. Roberto Vinicio Ruiz, coordinator, IV Business Forum of the Americas, March 16-18, 1998, San José, Costa Rica

We have truly come together in Central America with democratization, pacification, and now economic integration. The overall economic platform is growing more homogeneous. This regional integration will yield regional investment, and that is going to yield results."

Dr. Fernando Garcia, Minister of Economy, Honduras

All the economy ministers of Central America are meeting together at least twice a month. We are in an intense process of economic integration. Guatemala and El Salvador are going so far as to discuss complete elimination of customs duties at our frontier."

Dr. Eduardo Spericón, Vice-Minister of Economy, Guatemala

We are acting together to create a Central American economic bloc. This will greatly improve our competitiveness. We are already acting as a bloc in trade discussions with Chile and with the Dominican Republic."

Dr. Sergio Nuñez, Vice-Minister of Economy, Honduras

We must all work together in Central America. This is a decision we have already taken and we are firmly committed to. We are armed with a vision of a joint future for Central America."

Dr. Eduardo Ayala, Vice-Minister of Economy, El Salvador

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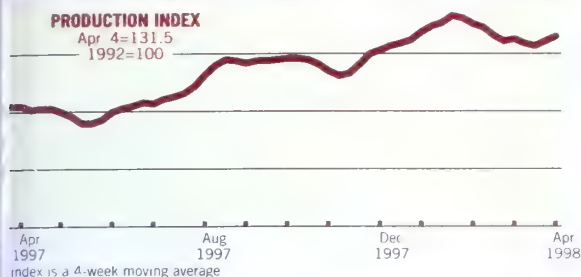
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Business Week Index

PRODUCTION INDEX

Change from last week: 0.3%
Change from last year: 4.7%



production index continued to climb for the third week in a row. Before season of the four-week moving average, the index was up 1%, to 133.131.7. After seasonal adjustment, all ten components were up. Both truck and lumber production rose 3.7%. Rail-freight traffic was up 1.9% as freight and 350,131 carloads. The Association of American Railroads reported a 1% first quarter for freight railroads in both the U.S. and Canada.

Production index copyright 1998 by The McGraw-Hill Companies

ADING INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
CK PRICES (4/13) S&P 500	1109.69	1122.70	50.4
PORATE BOND YIELD, Aaa (4/10)	6.64%	6.67%	-14.2
KEY SUPPLY, M2 (3/30) billions	\$4,123.8	\$4,123.1r	6.2
IAL CLAIMS, UNEMPLOYMENT (4/4) thous.	308	310r	-5.2
RTGAGE APPLICATIONS, PURCHASE (4/10)	287.3	248.8	63.0
RTGAGE APPLICATIONS, REFINANCE (4/10)	1,684.2	1,206.3	490.7

Sources: Standard & Poor's, Moody's, Federal Reserve, Labor Dept., Mortgage Assn. (Index: March 16, 1990=100)

TEREST RATES

	LATEST WEEK	WEEK AGO	YEAR AGO
ERIAL FUNDS (4/14)	5.47%	5.40%	5.61%
IMERCIAL PAPER (4/14) 3-month	5.47	5.45	5.71
TIFICATES OF DEPOSIT (4/15) 3-month	5.58	5.56	5.73
ED MORTGAGE (4/10) 30-year	7.12	7.23	8.27
USTABLE MORTGAGE (4/10) one-year	5.76	5.79	6.06
ME (4/10)	8.50	8.50	8.50

Sources: Federal Reserve, HSH Associates, Bloomberg Financial Markets

PRODUCTION INDICATORS

	LATEST WEEK	WEEK AGO	YEARLY % CHG
STEEL (4/11) thous. of net tons	2,174	2,218#	4.6
AUTOS (4/11) units	99,605	118,525r#	-13.1
TRUCKS (4/11) units	117,430	152,372r#	-12.9
ELECTRIC POWER (4/11) millions of kilowatt-hrs.	NA	58,695#	NA
CRUDE-OIL REFINING (4/11) thous. of bbl./day	14,945	14,641#	5.2
COAL (4/4) thous. of net tons	21,424#	22,103	16.1
LUMBER (4/4) millions of ft.	481.4#	476.0	-1.3
RAIL FREIGHT (4/4) billions of ton-miles	27.1#	27.6	5.0

Sources: American Iron & Steel Institute, Ward's Automotive Reports, Edison Electric Institute, American Petroleum Institute, Energy Dept., WWP1, SFP2, Association of American Railroads

PRICES

	LATEST WEEK	WEEK AGO	YEARLY % CHG
GOLD (4/15) \$/troy oz.	307.200	308.800	-9.6
STEEL SCRAP (4/14) #1 heavy, \$/ton	133.50	134.50	0.0
COPPER (4/10) ¢/lb.	81.7	80.9	-26.7
ALUMINUM (4/10) ¢/lb	68.0	68.8	-10.5
COTTON (4/11) strict low middling 1-1/16 in., ¢/lb.	60.00	65.17	-13.1
OIL (4/14) \$/bbl.	14.82	14.93	-24.1
CRB FOODSTUFFS (4/14) 1967=100	228.43	228.54	-6.0
CRB RAW INDUSTRIALS (4/14) 1967=100	298.52	298.39	-10.3

Sources: London Wednesday final setting, Chicago market, Metals Week, Memphis market, NYMEX, Commodity Research Bureau

FOREIGN EXCHANGE

	LATEST WEEK	WEEK AGO	YEAR AGO
JAPANESE YEN (4/15)	129.30	132.19	125.70
GERMAN MARK (4/15)	1.80	1.82	1.73
BRITISH POUND (4/15)	1.69	1.67	1.62
FRENCH FRANC (4/15)	6.03	6.09	5.81
ITALIAN LIRA (4/15)	1776.0	1794.5	1701.8
CANADIAN DOLLAR (4/15)	1.44	1.42	1.40
MEXICAN PESO (4/15) ¹	8.467	8.510	7.893
TRADE-WEIGHTED DOLLAR INDEX (4/15)	109.9	110.8	106.6

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound in dollars. Trade-weighted dollar via J.P. Morgan.

v data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense
1=Western Wood Products Assn. 2=Southern Forest Products Assn 3=Free market value NA=Not available r=revised NM=Not meaningful

THE WEEK AHEAD

DAILY RETAIL REPORTS

Monday, Apr. 21 ▶ In a week that contains economic news, the financial markets focus on the weekly retail reports, especially after the Commerce Dept. said March retail sales fell 0.1%. The Bank of Tokyo-Mitsubishi/Schroder Wertheim report, released at 9 a.m., and the IJR Red-Report, due at 2:15 p.m., will gauge buying for the week ended Apr. 18. Survey results vary because each analyzes data from different store chains. For the week of Apr. 11, the last shopping days before Easter, the Mitsubishi survey showed sales so far in April were up 1.4%. In March, while the Redbook report said sales rose 3.8%.

FEDERAL BUDGET

Tuesday, Apr. 21, 2 p.m. EDT ▶ The U.S. Treasury is likely to report a budget deficit of \$15 billion for March, says the median survey of economists surveyed by Standard & Poor's MMS, a division of The McGraw-Hill Companies. Washington posted a gap of \$21.3 billion last March. April, when most Americans settle their tax bills, will give the best reading of how much in the black the federal government will be in fiscal 1998 which ends in September. So far, though, the deficit is running \$34 billion less than in fiscal 1997. The nonpartisan Congressional Budget Office has projected a surplus of \$18 billion this year, and Congress and the White House are now

wrestling with how to spend any windfall. On Apr. 10, however, the Federal Reserve warned that forecasting the federal surplus is difficult because estimating future tax receipts is a complex task.

UNEMPLOYMENT CLAIMS

Thursday, Apr. 23, 8:30 a.m. EDT ▶ New claims for state unemployment benefits probably jumped to 325,000 in the week ended Apr. 18. Claims were running at a very low four-week moving average of 310,000 in early April. Although state offices did not close in the week of Apr. 11, unemployed workers may have held off applying for benefits until after the Easter and Passover holidays.

This Week, Online

Business Week presents frequent live conferences and chats on America Online—your opportunity to ask questions about timely topics.

Sunday

Work and family—a delicate balance. Azriela Jaffe, counselor to entrepreneurial couples, can help you cope.

Apr. 19

9 p.m. EDT in BW Online's Conference Room

Thursday

Investing in the Internet: Bill Burnham, Piper Jaffray's senior research analyst for E-commerce, has tips for you to click on.

Apr. 23

9 p.m. EDT in BW Online's Conference Room

B-Schools

Tuesday, and it's Harvard—the grand finale of our series of chats with MBA students at top campuses.

Apr. 21

8 p.m. EDT in BW Online's Conference Room

AOL keyword: BW Talk

Transcripts of all conferences are available for downloading from the BW Online area on AOL soon after each event.

Index to Companies

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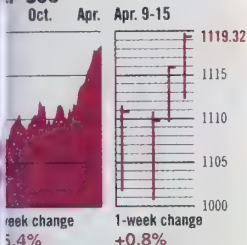


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Investment Figures of the Week

STOCKS

S&P 500



COMMENTARY

A bright week for U.S. financial markets, with equities continuing their record-setting advance. The Dow Jones industrial average climbed for 15 days straight, aided by bank mergers and strong earnings news. Remarks on Apr. 15 by Treasury Secretary Robert Rubin eased the concerns of bond traders, who were worried that the Group of Seven would take actions hurt the dollar. Generally favorable economic news, such as stability in consumer prices, and bond prices in check.

U.S. MARKETS

	Latest	% change Week	Year
Dow Jones Industrials	9162.3	3.0	37.2
NASDAQ Combined Composite	1863.3	3.1	54.0
S&P MidCap 400	377.1	2.8	50.0
S&P SmallCap 600	204.0	3.0	48.6
S&P SuperComposite 1500	240.1	1.8	47.0

SECTORS

	Latest	% change Week	Year
Bloomberg Information Age	339.6	2.4	49.5
S&P Financials	140.2	2.6	64.8
S&P Utilities	245.8	0.5	33.4
PSE Technology	351.6	3.6	46.7

FOREIGN MARKETS

	Latest	% change Week	Year
London (FT-SE 100)	6074.1	0.3	41.4
Frankfurt (DAX)	5388.5	2.3	60.7
Tokyo (NIKKEI 225)	16,299.3	-0.5	-9.6
Hong Kong (Hang Seng)	11,371.1	0.5	-9.6
Toronto (TSE 300)	7817.7	3.3	34.8
Mexico City (IPC)	4991.0	1.4	30.2

FUNDAMENTALS

	Latest	Week ago	Year ago
S&P 500 Dividend Yield	1.45%	1.40%	1.95%
S&P 500 P/E Ratio (Last 12 mos.)	27.7	27.9	19.6
S&P 500 P/E Ratio (Next 12 mos.)*	21.9	21.8	15.7
First Call Earnings Surprise*	2.88%	1.53%	3.28%

TECHNICAL INDICATORS

	Latest	Week ago	Reading
S&P 500 200-day average	973.0	968.6	Positive
Stocks above 200-day average	65.0%	66.0%	Neutral
Options: Put/call ratio	0.64	0.53	Neutral
Insiders: Vickers Sell/buy ratio	2.79	2.64	Negative

Data: Bloomberg Financial Markets; *First Call Corp.

BEST-PERFORMING GROUPS

	Last month %	Last 12 months %
Invest. Banking/Bkrge.	17.4	Broadcasting 115.5
Chemicals	15.1	Homebuilding 110.3
Photography/Imaging	14.6	Personal Loans 102.6
Money Center Banks	14.1	Specialty Appr. Retailers 101.8
Automobiles	13.6	Invest. Banking/Bkrge. 99.7

WORST-PERFORMING GROUPS

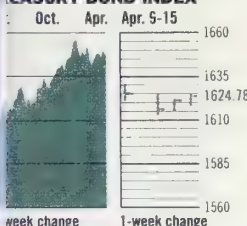
	Last month %	Last 12 months %
Toys	-10.9	Shoes -25.9
Food Chains	-8.3	Metals -22.3
Tobacco	-7.8	Engineering & Constr. -12.1
Drug Chains	-4.7	Gold Mining -11.6
Leisure Time	-4.6	Photography/Imaging 1.4

BLOOMBERG MONEY FLOW ANALYSIS

Rebound ahead? Stocks with most significant buying on price weakness	Price	1-month change
Oracle	28 1/2	-1 1/8
AT&T	64 7/8	-5/16
Telebras-ADR	130 3/8	-7/8
Lockheed Martin	111 13/16	-2 13/16
Merck	125	-4 1/2
U S West Communications Group	51 9/16	-3 1/16
Decline ahead? Stocks with most significant selling on price strength	Price	1-month change
Microsoft	88 7/16	6 7/16
WorldCom	44 53/64	2 5/16
Pfizer	99 1/16	11 1/16
Dell Computer	68 3/8	5 1/16
PeopleSoft	53 7/8	3 1/16
Centocor	41 1/2	2 15/16

INTEREST RATES

TEASURY BOND INDEX



Bloomberg Financial Markets

KEY RATES

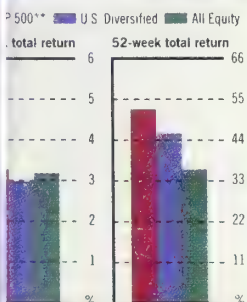
	Latest week %	Week ago %	Year ago %
MONEY MARKET FUNDS	5.10	5.11	5.04
90-DAY TREASURY BILLS	5.06	5.07	5.29
6-MONTH BANK CDS	5.08	5.06	5.18
1-YEAR TREASURY BILLS	5.35	5.28	5.99
10-YEAR TREASURY NOTES	5.59	5.53	6.90
30-YEAR TREASURY BONDS	5.88	5.84	7.11
LONG-TERM AA INDUSTRIALS	6.47	6.41	7.59
LONG-TERM BBB INDUSTRIALS	6.92	6.87	7.96
LONG-TERM AA TELEPHONES	6.73	6.69	7.82

BLOOMBERG MUNI YIELD EQUIVALENTS

Taxable equivalent yields on AAA-rated, tax-exempt municipal bonds, assuming a 31% federal tax rate.

	10-yr. bond Latest week	Last week	30-yr. bond Latest week	Last week
GENERAL OBLIGATIONS	4.45%	4.43%	5.05%	5.03%
PERCENT OF TREASURIES	79.60	80.32	85.90	86.24
TAXABLE EQUIVALENT	6.45	6.42	7.32	7.29
INSURED REVENUE BONDS	4.61	4.57	5.25	5.22
PERCENT OF TREASURIES	82.46	82.86	89.30	89.50
TAXABLE EQUIVALENT	6.68	6.62	7.61	7.57

MUTUAL FUNDS



Morningstar, Inc.

EQUITY FUNDS

Leaders	Four-week total return %	Laggards	Four-week total return %
Lexington Strat. Invmnts.	23.2	Capstone New Zealand	-11.2
Gabelli Gold	17.8	Lexington Troika Russia	-9.2
Am. Cent. Global Gold	17.2	DFA Japanese Small Co.	-7.8
Pioneer Gold C	17.1	Dreyfus Aggressive Growth	-6.9
Evergreen Prec. Metals B	16.9	Profunds UltraBear Serv.	-5.7
Leaders	52-week total return %	Laggards	52-week total return %
Delaware Aggressive Gr. A	105.0	U.S. Global Investors Gold	-52.0
Fidelity Select Brokerage	93.0	Matthews Korea I	-47.9
FMI Focus	90.9	Midas	-46.5
Munder Micro-Cap Equity Y	89.6	Morgan Stan. Asian Grth. C	-45.8
Weitz Hickory	88.9	Morg. Stan. Inst. Asia Eq. A	-45.4

EQUITY FUND CATEGORIES

Leaders	Four-week total return %	Laggards	Four-week total return %
Precious Metals	14.0	Pacific/Asia ex-Japan	0.1
Natural Resources	6.1	Health	0.2
Europe	5.6	Diversified Pacific/Asia	0.3
Financial	5.4	Japan	1.8
Foreign	5.3	Domestic Hybrid	1.9
Leaders	52-week total return %	Laggards	52-week total return %
Financial	65.0	Pacific/Asia ex-Japan	-29.5
Communications	61.9	Precious Metals	-25.9
Large-cap Growth	49.9	Diversified Pacific/Asia	-20.3
Unaligned	48.3	Diversified Emerging Mkts.	-5.3
Small-cap Blend	48.0	Japan	-4.1

are as of market close Wednesday, Apr. 15, 1998, unless otherwise indicated. Industry include S&P 500 companies only. Fundamentals, technical indicators, Bloomberg money

flow analysis, and mutual fund returns are as of Apr. 14. For a more detailed explanation, write to us or E-mail figures@businessweek.com. NA=Not available **Vanguard Index 500 Fund

BIG BANKS, BIG PROBLEMS

Size matters. But is bigger better in banking? That is the key question behind the recent rush to mega mergers in the banking industry. As banks approach the \$1 trillion mark in size, the benefits are clear: cutting costs, improving technology, and cross-selling products to more customers. But so are the problems.

Regulation becomes more problematic. Consolidation is doubling the number of TBTF (too big to fail) banks that regulators in the past have kept alive no matter what the cost to taxpayers. According to the Federal Reserve Bank of Minneapolis, there were 11 TBTFs in 1984 with assets of \$38.2 billion or more. By 1997, the number had reached 21 and was growing. Why so much consolidation? Banking industry assets are barely growing. There is now more money in mutual funds than in bank deposits. The result? Banks are leveraging their asset base more than ever (page 32).

To recapture their historic position, banks are linking up

with partners in insurance and equities. Convergence means all kinds of assets—stocks, insurance, consumer loans, corporate finance, mortgages—into one financial stew. The result? Big though they may be, banks are riskier enterprises than ever before.

Record-high stocks, the “cheap” money of the '90s, make bank mergers appear relatively painless. They aren't. Problems are inevitable, and Washington should begin to protect taxpayers from a replay of the 1980s' savings and loan crisis. Shareholders and managers shouldn't be saved simply because their banks are TBTF. The Minneapolis Fed's suggestion that Congress amend legislation to cut back the de facto government guarantee for uninsured depositors and creditors is a good start. It shifts the burden of risk from the taxpayers to those big players capable of monitoring bank behavior and protect their own interests. It's also time to merge the agencies overseeing banking. Size changes everything.

MAKING THE EURO WORK

The euro is an audacious experiment of historic proportions. In one bold move, the creation of a single currency makes Europe once again a contender for global economic leadership. If the euro delivers on its promise to remake Europe into a competitive powerhouse, the fulcrum of economic power in the 21st century could eventually shift back to the Atlantic basin, away from the now troubled Pacific Rim.

But first, hard political work to lay the foundation for the euro has to be done. Europe must break down workplace, tax, and regulatory rigidities before the new currency can unite the region. The success of the euro lies in the hands of politicians, not economists, central bankers, or chief executives.

A conspiracy of silence threatens the euro's success. To date, Europe's politicians have portrayed the advent of the euro as a mere accounting device, entirely financial in nature. Once monetary and fiscal policies are centralized and locked in place with a single currency, individual governments will have power over only taxes, labor, and regulation. Unless they use these levers to promote growth, the euro will fail (page 90).

So far, most European politicians have shown little courage. In curbing budget deficits for the runup to a single currency, they raised taxes instead of cutting government spending, thereby hurting job creation. They bowed to union pressure and refused to make work hours more flexible. They rebuffed corporate requests for help in lowering their costs.

European corporations are not waiting for the euro. By threatening to shift new investment to Eastern Europe and the U.S., European companies have persuaded local unions to curb wage demands. Corporate profits have been strong for three years, and European stock prices are soaring.

The euro is Europe's last best chance to vie again for global

leadership. The currency can be the driving force that makes Continental corporations globally competitive. Or not. Prime Minister Margaret Thatcher withstood more than a decade of strong political opposition to her efforts to make Britain competitive. European politicians have shown no such grit. But the must. Japan once towered over the global economy, only to slip into economic despair because its politicians could not make hard economic decisions. The saddest sight in Western Europe today is the thousands of its best and brightest abandoning the countries for Silicon Valley and London.

There is no doubt that should the euro succeed, it will make Europe a much more formidable—and welcome—competitor to the U.S. By 2003, when marks, francs, lire, and pesetas are totally replaced, the euro could begin to rival the dollar as a major reserve currency. A new euro-denominated capital market could develop. The \$6.4 trillion euro economy, second only to that of the U.S., will probably run big trade surpluses and be a net creditor to global financial markets. The result? To the U.S., the world's largest debtor, running the world's biggest current-account deficits, could easily find that other nations are less willing to hold dollars or dollar-denominated assets. The fear that the U.S. gets on its chronic trade deficits and its high savings rate could soon end. This would not be a bad thing. A strong euro might puncture America's boastful triumphalism and force the country to deal with some of its serious problems.

Creating a new common currency is an extremely difficult task. It took the U.S. decades to accomplish. Individuals relinquish their familiar stores of value very reluctantly. Europe's political leaders must show their people they can do what is necessary to unleash the great potential of the euro. This is a moment in history all of Europe must seize.

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Bill and Linda had cabin fever.

Bad.

Bill said, "I wish spring would get here."

Linda said, "I wish we'd get to spring." Twelve hours later they were in their Ford Taurus, putting all 200 horses out to graze below swaying palms.

Was it impulse

or instinct?

Either way, Taurus



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